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CONSUMER BENEFITS ASSOCIATED WITH THE CHANGING FINANCIAL SERVICES ENVIRONMENT

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HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER AFFAIRS

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

NINETY-NINTH CONGRESS

SECOND SESSION

ON

WHAT BENEFITS WILL FLOW TO THE CONSUMER SHOULD CONGRESS MODERNIZE THE LEGAL FRAMEWORK OF THE FINANCIAL WORLD? DOES THE CONSUMER REALLY WANT AND DEMAND ONE-STOP FINANCIAL SERVICES?

MAY 7, 1986

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

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CONSUMER BENEFITS ASSOCIATED WITH THE CHANGING FINANCIAL SERVICES ENVIRONMENT

WEDNESDAY, MAY 7, 1986

U.S. SENATE, COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS, SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER AFFAIRS,

Washington, DC.

The subcommittee met at 9:30 a.m., in room SD-538, Dirksen Senate Office Building, Senator Slade Gorton (chairman of the subcommittee) presiding.

Present: Senators Gorton, Garn, Hecht, D'Amato, Proxmire, and Cranston.

OPENING STATEMENT OF SENATOR GORTON

Senator GORTON. This morning we will hear testimony on the driving forces behind and the consumer benefits asserted to be derived from the changing financial services arena.

Before the Senate passage of S. 2851, the Financial Services Competitive Equity Act of 1984, the Banking Committee held over 50 hearings concerning the changes taking place in the delivery of financial services. Those hearings examined those changes from the providers' point of view and focused on what those businesses thought the legal framework would look like in response to the changes.

Today's hearing is not intended as just another forum for the financial services players to present their wish list. This morning we will take a different approach to the same debate and issues. Instead, we will review from the consumers' perspective the changes which are taking place and determine what congressional responses are appropriate.

The questions we will address are simple and straightforward. What benefits will flow to the consumer should Congress modernize the legal framework of the financial world? Does the consumer really want and demand one-stop financial services?

Senator Proxmire indicated last week that he is not convinced of the consumers' desire for a financial supermarket. He said, "In actuality, most consumers want better service, not more services." I'm sure we will hear more from Senator Proxmire on this matter.

First, we will hear from Ken Kehrer, a consultant and researcher of financial services.

Originally, a representative of the Stanford Research Institute [SRI] was also scheduled to testify. That company helped design the cash management account for Merrill Lynch, an account which has millions of customers and has attracted more than $70 billion in a few years. Although SRI agreed to testify, it unfortunately was not able to clear its testimony in time for today's hearing.

Second, Sears and Beneficial, two active and aggressive financial services providers, will outline what they anticipate for the future, preferences of the consumer, and how their organizations are addressing their customers' desires.

Finally, a community bank from Kansas and a thrift from Illinois will discuss their respective roles in the changing financial marketplace.

No group was intentionally excluded from this hearing. If further interest is demonstrated, additional hearings on consumer preferences for financial services will be held.

Senator Proxmire.

OPENING STATEMENT OF SENATOR PROXMIRE

Senator PROXMIRE. Thank you, Mr. Chairman.

As you say, Mr. Chairman, the announced purpose of these hearings is to conduct oversight "on the driving forces behind and consumer benefits associated with the changing financial services environment."

Now that's an exceedingly vague description of the subject matter. To make matters even more confusing, we didn't receive the testimony or even the witness list until late yesterday afternoon, nor were any staff memos circulated to explain in more detail what these hearings were intended to accomplish. As a result, neither I nor other members on our side of the aisle nor our staffs have had time to prepare for these hearings as we should.

In the brief time I have had to examine the testimony it appears that the central purpose of these hearings is to make a case for dismantling the traditional separation between banking and other lines of financial and commercial activity. Certainly all of the witnesses seem to echo that theme. There do not appear to be any contrary points of view.

Because the witness list has been stacked, the credibility of this hearing is open to serious question.

One of the myths perpetuated by those who sing the praises of nonbank banks or family banks as some prefer to call them is the consumers are demanding new and innovative services from their banks and that if banks are not supplied these new services they will wither on the vine and eventually go out of business.

Mr. Chairman, this myth has been effectively exploded in two recent studies of what consumers really want from their banks, one done on the west coast and one done on the east coast. In both cases, these studies found that new and innovative services rank last—last or next to last—in things consumers want from their banks. Both studies agree that the overwhelming number of consumers want better delivery of basic banking services, not new services.

I can't think of a more damaging development we could have in this country than to permit nonbank banks to move in on our credit markets. We have the best credit markets in the world. We're very proud of our credit markets. They have done extremely well. They are recognized in other countries as their envy. Of course, our credit markets are unique because they are featured by a very large number of independent banks, 11,000 independent banks, not just 4, 5, or 6 as most countries have that dominate the credit markets.

What happens when we come in with a nonbank bank? Well, they take the deposits away from the local banks, the community banks, and those community banks don't have the resources that they had before.

Before I came to the Senate I was the president and half owner of a printing company. We relied very strongly on the local bank which was enormously helpful to us. And you know the overwhelming majority of businesses in this country, the small businesses, aren't able to hire the McKinsey & Co. and the other great and very fine financial advisers. They rely on their bank for advice, their local bank in their local community. There's a commitment to the community.

You get these big Sears operations and others that come along and attract the capital out of the local community and there's no questions that as time goes on the local community is going to suffer; the businesses in the local community aren't going to have either the financial resources or the direct advice of their banker to assist them because the banks will follow the same path they have followed in so many other countries. They will become branches of big central banks located elsewhere.

Mr. Chairman, I ask unanimous consent that the two studies to which I referred be printed in the record of these hearings. Hopefully, these studies will help to balance an otherwise woefully unbalanced record.

Senator GORTON. They will be so included.

[The following studies were subsequently submitted for the record:]

BANK ATTRIBUTE DETERMINANCE: INITIAL FINDINGS IN THE CONSUMER CHOICE PROCESS

by

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ABSTRACT

Traditionally, the financial services industry has considered convenience and location to be the attributes which determine consumers' choice of one bank over another. This study of 900 households has found that consumers determine their choice of banks on the basis of perceived friendly and efficient service and the extent to which the bank has a personal interest in them. The marketing implications of this change in consumer choice behavior are important, as are the relative importance of other attributes such as convenient location, innovativeness, and some pricing issues.

Introduction

With deregulation, the increase in non-bank competitors and the increasing sophistication of today's financial services consumer has increased the bankers' need to understand how consumers select one financial institution over another. The issue is identification of the characteristics of a bank that make a consumer more or less likely to have a preference. In the past, most research indicated that the majority of consumers chose their bank on the basis of location [1, 4, 5]. That is, most consumers choose the bank which is closest to either their home or work. Today's increasing sophisticated customer appears to be using other attributes to choose one institution over another. This paper will present the results of a recent study investigating the determinant attributes in the bank selection decision.

With the deregulated and newly competitive environment for bank services, attracting newcomers and bank switchers has become an increasing preoccupation for the bank marketing team. The careful use of persuasive advertising, coupled with personal selling has become a standard part of the marketing arsenal for most banks, and consumers are responding by switching from one institution to another, and by being more selective in the initial banking decisions. However, merely advertising, or extending the personal selling effort of the institution will not guarantee success in the marketplace unless the advertising or personal selling effort is targeted at the issues that today's consumer considers relevant in their choice of a financial institution. If a bank does not understand what criteria are used by consumers in that bank choice decision, then valuable marketing resources may be wasted and the marketing effort will not be effective in achieving the goals of the institution [3].

Bank Characteristics

In this study, consumers were asked to evaluate the importance of eight bank characteristics. The characteristics were chosen after a review of the banking literature, and after consultation with bank marketing officers. The eight characteristics are descriptive of attributes that consumers are known to consider when making a bank choice decision [1, 4, 5, 7, 9]. A brief discussion of each of the characteristics and the rationale for including that characteristic follows:

The first characteristic is financial soundness/sound management. It is common knowledge that consumers choose banks over other types of financial institutions at least partially because of the low risk associated with banks. It is logical to assume than an important characteristic of a bank would be how financially sound that bank is, and how well managed it is perceived to be. With the recent sharp increase in bank failures, the arguments for including this characteristic become even more compelling.

The second characteristic is conveniently located branches and hours. Since this characteristic has traditionally been the determining one for many bank choice decisions [6], it should logically be included in any new study of bank choice. Also, one of the goals of the study was to evaluate the continued importance of this characteristic, particularly since there are now so many nontraditional financial institutions available to the consumer, such as bank-by-mail money market funds, and single location asset management accounts offered by brokerage houses.

The next characteristic is high interest payments for savings products. With the entry of thrift institutions into the traditional banking market, along with other on-demand savings account types for non-traditional institutions, the amount of interest paid by banks for savings products was a logical

characteristic to evaluate, since consumers may use interest rates as a decision criterion.

The fourth bank characteristic included in the study was the reasonableness of demand deposit account requirements and fees. Even in highly competitive markets, minimum balance requirements, transaction fees, and other demand deposit account characteristics may vary widely from one institution to another and from one institutional type to another. Since this is the "price" dimension of the service, it is logical that it would be a characteristic that consumers might use to choose one bank over another.

The next characteristic tested as important to consumers was friendly and efficient service. Most consumers are averse to long teller lines, long waits a drive-up windows, and other delays in transacting their banking business. At the same time, consumers are sensitive to the friendliness of the bank personnel with whom they come in contact. Every bank has a story of a (former) customer who was offended by a rude or impersonal employee and took their business elsewhere as a result.

The sixth bank characteristic was favorable interest charges on loans. This "price" dimension of a bank's services might influence the choice made by certain consumers, so it was considered valid for inclusion in the study.

Another characteristic of concern to consumers was the personal interest taken in customers. The success of personal banker programs, particularly when they are used by larger institutions argues that consumers are sensitive to being known by and knowing someone in their bank. A recent article in "Ms." magazine encouraged women to "get to known you banker before you need his or her special attention [3]." Clearly, the continued success of community banks is at least partially attributable to the perception on the part of consumers that a smaller bank will provide more personal service than will a larger institution.

The last bank characteristic included in the study was the presence of up-to-date and innovative services. The explosion of bank services allowed by the deregulation of the banking environment has allowed consumers much more choice in the kinds of services they use. Since consumers are more aware of the services that are available to them, it was logical that they might be sensitive to banks which were perceived as being innovative and offering the latest services.

The Study

A mail survey was conducted for this study. The instrument and methodology was pretested on 100 randomly selected households. Results from the pretest suggested few changes in the original questionnaire. The pretest did, however, aid the researchers in verifying the eight most salient attributes in the bank choice decision and did not suggest any new attributes.

A survey instrument, a cover letter explaining the purpose of the study, and a business reply envelope were sent to 3,830 households. Of the 3,830 surveys, 13 were undeliverable, for a net mailing of 3,817. There were 807 useble responses, for a survey response rate of 21.1%.

The survey instrument asked the primary wage earner in the household to respond to items concerning the household usage of different types of financial institutions, the importance of the eight bank characteristics discussed earlier, the perception of the respondent with regard to the similarity of financial institutions on the eight characteristics, and demographic detail. Anonymity was insured for all respondents.

Financial Institutions Usage

Nearly all the respondents used the services of some financial institution. Only 1.7% reported that they did not use any financial

institution, these were deleted from further analysis. Of the respondents who used some type of financial institution, 98.4% used a bank, 33.2% used a savings and loan, 23.7% used a credit union, and 8% used some other type of financial institution, such as a money market fund. The percentages add to more than 100% because of multiple institution usage by some respondents.

The respondents were asked to identify (by name) the financial institution where they used seven types of services: non-interest demand deposit accounts, interest paying demand deposit accounts, passbook/statement savings accounts, certificates of deposit, money market accounts, individual retirement accounts, and trust accounts (see Table 1). The respondents were also asked to distinguish between their primary (most frequently used) financial institution and accounts in other institutions. The respondents were also asked how long they had been using their primary financial institution. The average primary financial institution had been used 15.2 years, with a range from 1 to 67 years. The average usage of the non-primary institution was 10.8 years, with the range from 1 to 61 years.

TABLE 1

AGGREGATE ACCOUNT TYPE USAGE

Type of Account	Primary No.	Primary %	Other No.	Other %	Total No.	Total %
Non-interest Checking	526	65.2	137	17.0	663	82.2
Interest Checking	325	40.3	81	10.0	406	50.3
Passbook/Statement Savings	489	60.5	166	20.5	655	81.2
Certificates of Deposit	262	32.4	95	11.8	347	44.2
Money Market Account	170	22.1	48	5.0	218	27.0
IRA	162	20.1	33	4.1	195	24.2
Trust Account	54	6.7	13	1.6	67	8.3

NOTE: The percentages add to more than 100% due to multiple account usage.

Respondents' reported that, of their primary institutions, 32.2% presently offer automatic teller machines, 89.2% presently offer trust services, 46.7% presently offer brokerage services, and 96.2% presently offer individual retirement accounts.

Demographic Profile of Respondents

The households in this survey were predominantly composed of married people (71.2%). There were 2.69 people living in the average household, with the number of people ranging from 1 to 11. Slightly over three-fourths of the households (77.3%) owned their homes. The respondents were fairly well educated, with 71% of the primary wage earners having at least some college education. The average age of the primary wage earner in the households was slightly over 40. The total household income for the respondents averaged slightly over $20,000 per year. The respondents were a stable group, with the average household residing at the current address between 4 to 6 years. In short, the average respondent in this study is a settled, early middle-aged, married person with at least some college and a child still at home. (see Table 2).

TABLE 2

DEMOGRAPHICS OF RESPONDENTS

AGGREGATE EDUCATIONAL LEVEL

Educational Level	Percentage
Some High School	8.5
High School Graduate	20.5
Some College	26.8
College Graduate	44.2

TABLE 2--Continued

AGGREGATE AGE OF PRIMARY WAGE EARNER

Age Category	Percentage
Under 21	.6
21 to 29	16.8
30 to 39	24.9
40 to 49	16.3
50 to 59	16.1
over 60	23.4

AGGREGATE HOUSEHOLD INCOME

Income Category	Percentage
Under $10,000	11.0
10,000-19,999	22.6
20,000-29,999	25.0
30,000-39,999	19.5
40,000-49,999	10.5
over $50,000	11.4

AGGREGATE YEARS AT CURRENT RESIDENCE

Residence Years	Percentage
Less than 1 year	3.4
1 to 3 years	13.2
4 to 6 years	11.7
over 6 years	69.7

Characteristic Importance

The respondents were asked to rate the importance of the eight characteristics, or attributes, of financial institutions when evaluating the choice between one institution over another. The rating scale used was a one-to-five Likert-type scale, where 1 was "not very important" and 5 was "very important." The average rating for each of the eight attributes, as they affect the choice of a financial institution are presented in Table 3.

TABLE 3

ATTRIBUTE IMPORTANCE OF FINANCIAL INSTITUTIONS

Attribute	Attribute Importance Ranking
Financially sound/well managed	4.73
Conveniently located branches and hours	4.61
High interest on savings	4.35
Reasonable checking account requirements and fees	4.48
Friendly and efficient service	4.31
Favorable interest charges on loans	4.26
Personal interest in customers	4.25
Up-to-date and innovate services	4.07

Not surprisingly, the respondents rated financial soundness/sound management as the most important attribute for financial institutions. This result is consistent with the motive most customers have for using a financial institution in the first place: safety for their money. Friendly and efficient service was second most important, and reasonable demand deposit requirements was third. Interestingly, location--traditionally considered to be very important--was fourth. Interest payments for savings was fifth, and favorable interest charges on loans was sixth. A personal interest in customers was seventh. The last place attribute, in terms of importance, was up-to-date and innovative services. This indicates that, while respondents

did not necessarily think this attribute was unimportant, it was less important than the others in the set.

The results of the attribute importance ratings by the respondents indicates that people are still concerned for the safety of their money, and it is important to them to feel that a financial institution will provide safety and sound management of their assets. Even though many financial institutions have committed considerable resources to the development and the promotion of new services recently, the respondents in this study did not view that attribute as being as critical as the other, more traditional characteristics of financial institutions.

Characteristic Similarity/Dissimilarity

Respondents were also asked to compare the similarity of financial institutions with regard to the eight attributes. Once again, a 1 to 5 rating scale was used, where 1 represented "very similar" and 5 represented "very different." Thus, a "1" on an attribute, indicates that all financial institutions were very similar on that attribute. The average similarity/dissimilarity ratings for each of the eight attributes are presented in Table 4.

TABLE 4

ATTRIBUTE SIMILARITY/DISSIMILARITY OF FINANCIAL INSTITUTIONS

Attribute	Attribute Importance Ranking
Financially sound/well managed	2.67
Conveniently located branches and hours	2.61
High interest on savings	2.30
Reasonable checking account requirements and fees	2.78
Friendly and efficient service	2.68
Favorable interest charges on loans	2.64
Personal interest in customers	2.98
Up-to-date and innovate services	2.68

Though being financially sound and well managed was considered the most important attribute by the respondents, the respondents also perceived that financial institutions were most similar on that attribute. In other words, the respondents saw most financial institutions as being more or less equally financially sound and well managed. This perception is probably due at least in part to the regulatory climate which requires prudence in financial management, and the insurance programs such as the FDIC and FSLIC. Respondents saw most financial institutions as similar on the convenience of their locations and their hours. The two most dissimilar attributes, in the eyes of the respondents were friendly and efficient service and personal interest in customers. That is, the respondents perceive there being relatively greater differences among institutions on those two attributes than the others. Consumers also saw financial institutions as being relatively different in their willingness to offer up-to-date and innovative services.

Determinant Attributes

Determinant attributes analysis is the process by which the importance of an attribute (or characteristic) is combined with the perceived similarity or dissimilarity of different financial institutions on that attribute. Determinant attribute scores are the multiplicative product of the importance rating and the similarity/dissimilarity rating [2, 6, 8].

In this study, the possible range of determinant attribute scores was from 1 to 25 (1 to 5 for the importance rating scale multiplied by 1 to 5 for the similarity/dissimilarity rating scale). According to the theory [2, 6, 8], the higher the determinant attribute score, the more influential that attribute was in a customer's choice of a financial institution. The determinant attribute scores for the eight bank characteristics are presented in Table 5.

TABLE 5

DETERMINANT ATTRIBUTE SCORES AND RANKING
FOR FINANCIAL INSTITUTIONS

Attribute	Determinant Score	Ranking
Financially sound/well managed	11.60	4
Conveniently located branches and hours	11.51	5
High interest on savings	10.86	7.5
Reasonable checking account requirements and fees	12.45	3
Friendly and efficient service	12.99	1
Favorable interest charges on loans	11.24	6
Personal interest in customers	12.67	2
Up-to-date and innovative services	10.91	7.5

The attribute with the highest score was friendly and efficient service (12.99). It is this attribute—or more accurately, a customer's perceptions of an institution's performance on this attribute—which is most likely to determine the customer's choice of a financial institution. Even though being financially sound and well managed was the most important attribute, the perceived similarity among financial institutions with regard to this attribute caused it to be ranked fourth. In addition to friendly and efficient service being ranked as the most determinant attribute, respondents

ranked personal interest in customers as the second most determinant attribute. The two least determinant attributes were the innovativeness of the financial institution and the interest paid on savings products. The common wisdom and historically used location attribute scored only fifth in determinance in this study, indicating this customer group does not consider location to be determinant in their selection of a financial institution.

Implications of the Study

The implications of this study are quite clear. The bank customers in this study are more interested in the personal characteristics of their relation- ship with financial institutions than they are the issues of fees, financial soundness, or location. Innovativeness, which many financial institutions use as an important part of their promotional message, is considered least determinant of all the characteristics included in this study. While customers might want their financial institutions to be innovative, they do not use this characteristic as a rationale for choosing one institution over another.

As well, the mechanical aspects of the relationship between a customer and the financial institution they use is relatively unimportant as a determining factor in the selection of that financial institution. There may be two alternative explanations for this attribute. First, the consumers may really see costs associated with demand deposit accounts and the interest charged for loans as being relatively unimportant when compared to the availability of friendly and efficient service. That is, a customer may be willing to "pay" for that friendly service with higher fees for bank products. The second explanation is that customers may believe that the newly competitive environment has forced all financial institutions to offer much the same rates and fees to the public. That is, bank services are commodity priced

rather than being priced differentially. Whether this is in fact true or not is irrelevant. If the customers perceive it to be true, then they will act on that perception. There is no evidence to support one or the other of the alternative explanations, but one fact remains: fees and interest charges were not the determining attributes in bank selection behavior for the sample of bank customers. The marketing implication of this information is clear as well. Financial institutions which allocate marketing resources to the promotion of free checking accounts, or low interest home improvement loans may not be spending their marketing dollars in the most efficient manner. While there are certainly consumers in the marketplace who will respond to such a marketing effort, there are other, more appropriate appeals which could be used.

The results of this study indicate that financial institutions should allocate marketing resources to the development of friendly and personal service and a personal interest in their customers. In addition, financial institution's need to promote these attributes as part of their overall advertising effort. Larger institutions particularly should devote marketing effort to the message that a bank need not necessarily be small to provide personal service or to have a personal interest in its customers. Testimonials and other forms of endorsement will provide a means of delivering this important message to customers. Small institutions should continue to use the natural advantage their size gives them in this competitive arena, and play on the already perceived notion that a small institution will more easily provide that personalized care that consumers want.

Conclusion

It isn't new services that financial institution consumers want, nor is it necessarily free checking accounts. The consumers in this study wanted to know that their financial institution could provide them with friendly and efficient service, and that their institution had a personal interest in them. Changing the focus of the marketing effort in the bank from an operations perspective to a consumer perspective is an important change that is necessary if financial institutions are to continue to be competitive. Training personnel in the importance of friendliness and concern for customers has become a cornerstone of any marketing effort.

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A NEW FOCUS ON RETAIL CUSTOMER VALUES

an article written exclusively for:

The JOURNAL OF RETAIL BANKING

by: Robert O. Metzger, Ph.D.
University of Southern California

and

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Indiana University - South East

March 1980

Teaser

Since deregulation began in 1980, pundits and consultants have been "bank bashing" because bankers have been too slow to develop the products and services consumers allegedly wanted and resisted the obvious solution to their marketing problems, i.e. translating to the merchandising of a broad array of financial services products. Two new retail bank customer research projects, however, fly right in the face of much of what has been recommended. Customers, it would seem, are not interested in complex new products or sophisticated new services. What they want, and appear less and less able to get, is personalized attention and recognition. They certainly do not perceive of their banker providing much else.

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A New Focus on Retail Customer Values

by: Robert O. Metzger
and
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Recently, the results of two major research studies on bank retail customer perceptions and needs were completed. One study was performed by Cwin and Lindgren of the University of Virginia, and consisted of interviews with over 800 retail depositors on the East Coast. The second study was performed by the authors on the West Coast and consisted of detailed, extensive written questionnaires from almost 900 retail customers of an upscale community bank. The basic findings of both surveys are very similar and appear to contradict strongly many of the strategic and marketing actions being taken by a majority of retail bankers today. The purpose of this article is to provide some detail from one of those studies and to use the findings to explore the strategic and marketing implications for retail bankers.

Introduction

Since deregulation began to envelope the banking industry in 1980, a number of pundits have berated bank management for its lack of marketing orientation, customer needs sensitivity and imagination; and, have compared it generally and specifically to CPA management in the mid-70s, struggling to survive amid much more sophisticated, customer oriented competition. These industry analysts and consultants compared retail banking with merchandising and talked freely and passionately about boutique banks and bankers learning how to manage financial supermarkets. Slowly the groundswell built until 1983 when many in the industry were devoting their R&D budgets to new products and "High Tech" EFT systems development. Home banking and financial counseling became the new buzz words, and a bank really wasn't "de rigeur" unless the branch personnel had been subjected to a course in personal money management or telemarketing. Banks which had never had an MBA on the staff suddenly were developing full fledged marketing departments. Market research firms and sales training consultants were hiring their own consultants to advise them on what to do with the fees they were earning. But something else appears to have been happening simultaneously. Retail customers were becoming less enamored with their bankers. Their service charges were being increased, branch staff was being cut to acknowledge the increased productivity provided by newly installed automation; or, loan officers were being pulled from branches into "hub" offices twenty miles away. A number of major banks, in an effort to cut personnel costs, have replaced customer service specialists answering telephones with automated recording devices to take messages. Further, many of the new products and services developed were so involved that customer service personnel couldn't explain them to the satisfaction of depositors. In the center of this financial services maelstrom, these two separate marketing studies were begun in late 1985 to better understand what the retail depositors really want from their banks. Those bankers who have just committed to home banking, CIRRUS and discount brokerage had better take heed. The results of these surveys raise the question that if a "High Tech" party was thrown right now for retail customers, who, if anyone, would come?

The West Coast Study

The authors developed a detailed product and services oriented questionnaire to test retail customer preferences and decision factors relative to their banking relationships. The basic questionnaire had been used and modified several times with various retail banks and thrift institutions. This latest version was developed for a $200MM community bank in California which serves a particularly affluent marketplace in an already affluent area of California. 1982 per capita income in the County is estimated in excess of $22,000 while the bank's retail customer income averaged in excess of $60,000 in 1985. The questionnaire was mailed to every retail checking account customer with a balance in excess of $1,000 (approximately 4,500 accounts) with the questionnaires segregated between those customers with balances in checking, NOW, money market checking or money market savings accounts between $1,000 and $9,999 and those with balances of $10,000 or more. This $1,000 cut off was a reflection of Pareto's Law at the bank, i.e. these customers represent that 20% of all accounts which, in turn, make up 80% of all retail

checking deposits.

The questionnaire posed 27 complex questions, principal among them being a review of 23 general retail banking services. Customers were asked whether or not these services were used at their primary financial institution. A similar review of some 13 specialized services not currently offered by the bank was performed also and customers were asked if they would use these services if their primary bank developed them. They included services such as investment counselling and home banking. Another set of questions reviewed the importance of 24 factors vis-a-vis the customer's original decision to open an account at the bank. Also tested were customer evaluations of the interest rates paid on various products; an identification of how and where customers learn about new financial services; how many and what kinds of accounts customers keep with various financial services institutions; and, a review of how customers invest their assets. While there were a number of detailed demographic questions raised, too, these are the ones which have the greatest bearing on current industry retail marketing and strategic activities; and, it is on these results that the authors will concentrate.

Customer Demographics

Some information should be provided on the demographic findings of this group due to its unusual affluency, education levels and employment patterns. Certainly similar research would provide somewhat different results in the Los Angeles barrio or the Upper East Side of Manhattan. The response of almost 900 customers from the original 4,500 was particularly robust. 60% of those responding provided the bank with additional hand written comments after filling in the very exhaustive questionnaire. The demographics of these retail depositors show that the largest single group, over 28%, are professional people. 66% are married, while over 80% own their own home. Over 65% of the respondents have a family income in excess of $50,000 and more than 25% have annual incomes in excess of $100,000. 92% stated that they have some college education, 69% are college graduates and 86.2% of the spouses have some college. 29% attended graduate schools. While 75% stated that they were between the ages of 35 and 64, fully 75% of the married respondents stated that they have no children living with them. Their children are either grown up and gone or away at school. **In spite of these income levels, over 50% of the spouses stated that they work fulltime and more than one in four of them is a professional (doctor, lawyer, dentist) also.**

Summary Findings

The authors found that in overwhelming proportions, **affluent retail bank customers perceive their primary bank to be principally a custodian of their liquid assets** close to home whereby they can have convenient access to them. Beyond this, these retail customers do not and **cannot** perceive of any other major relationship with their bank or its staff. They already have fixed relationships with pension and trust advisors, CPAs and tax attorneys, major brokerage houses and professional, full time investment advisors. After 50 years of being regulated out of these services, bankers are not thought of in this context nor do the vast majority of retail customer perceive that their banker would ever doing a credible job in these areas. To the contrary, **over 65% of these retail customers stated that they had absolutely no interest in any new products or services developed by their primary bank.** And, in many publicized areas such as home banking, telephone bill paying, tax and travel related services, at an average, while only 7-8% of the customers indicated that they would utilize these services if they were offered by their bank, up to 30% of all respondents stated that they absolutely would not seek such services from their bank even if they were developed. It is this vehemence of rejection more than anything else which communicates much of the customers' perceptions.

Finally, in summary, what is of importance to these key customers is the level of attention and recognition they receive when they do visit their bank. In the hype of the industry today, "High Touch" won over "High Tech" by a margin of 9 to 1!

Detailed Results

1. General Services Utilization

These checking account holders were asked: do they currently use any of some 23 typical bank services? The results appear below.

Service Offered	% Customers Use Service*	Heavy User Clusters
ATM Machines	57.6%	Singles, Professionals
Travellers Checks	56.8%	>$50K IncomeGroup
Overdraft Protection	54.0%	>$50K, Professionals
Safe Deposit Boxes	45.2%	>$50K, Homeowners
Bank-By-Mail	43.9%	>$50K, Professionals
Money Market Savings Accounts	41.0%	>$50K, Homeowners
Regular Savings Accounts	40.5%	Females
NOW Accounts	39.7%	>$75K,<$25K,Homeowners
Credit Cards	38.7%	>$50K IncomeGroup
Money Orders	33.6%	>$50K IncomeGroup
Personal Line of Credit	28.8%	>$50K IncomeGroup
Automated Balance Information	28.7%	>$50K, Females
Money Market Checking Accounts	28.2%	>$50K, Homeowners
Certificates of Deposit	20.2%	>$50K IncomeGroup
Auto Loans	17.6%	Males
Direct Deposit Services	16.3%	>$50K, Professionals
IRA Accounts	15.5%	Married, Professionals
Direct Deposit of Social Security	15.1%	Over 60 Group
Mortgage Loans	7.2%	Married
Automated Bill Paying Services	6.9%	Married, Professionals
Payroll Savings Plans	4.9%	$25-50K Group
Home Improvement Loans	3.3%	>$50K,Married
Telephone Bill Paying Services	<1.0%	N.A.(too few)

* These percentages reflect average responses across the multiple demographic cells tested.

2. Specialized Services Interest Levels

The respondents also were asked to state if they were interested in some 13 specialized services, many of them on the cutting edge of retail banking today. Specifically, customers were asked: if their bank developed these particular products, would they avail themselves of the service?

Service Offered	Customers Interested	Customers Rejecting*
Escrow Services	11.8%	10.6%
Estate Planning	12.3%	15.0%
Trust Services	9.0%	11.0%
Home Banking	9.0%	5.7%
Company Retirement Plans	3.1%	<1.0%
Tax Preparation Services	1.0%	26.0%
Tax Planning Services	10.0%	13.0%
Catalogue Merchandise Services	<1.0%	17.0%
Discount Brokerage	13.2%	14.3%
Stock Portfolio Management	<1.0%	18.2%
Investment Advisory Services	2.6%	14.3%
Will Preparation Services	15.0%	18.0%
Insurance Brokerage	8.5%	19.1%

3. Magnet Factors

Customers, then, were asked to state which factors were most important to them in the selection of their primary bank. The following is a list in descending order of importance and the 10 most important factors appear to coincide closely with the results of a recent Bank Marketing Association survey.

Factor	% Customer Feel Important*
Accuracy	96.8%
Quality of Overall Service	95.9%
Friendliness of the Staff	91.6%
Speed of the Teller Lines	90.1%
Insurance on Accounts	89.5%
Reputation of the Bank	88.4%
Branch Close to Home	86.0%
Expertise of Contact Officer	84.3%
Innovative Services	73.5%
Rates Paid on Deposits	73.3%
*****	
Bank Referred by Family Member	64.4%
Extended Hours	63.8%
Branch Close to Work	63.3%
ATM Machines	57.8%
Good Drive-Up Facilities	53.5%
Rates on Personal Lines	51.9%
Attractiveness of Bank Building	50.0%
Rates Paid on IRA Accounts	49.9%
Rates on Installment Loans	48.5%
Scope of the Branch Network	36.4%
Rates on Mortgage Loans	32.7%
Branch Close to Shopping	23.2%
Statewide Offices	20.7%
Referral by Bank Employee	20.5%

4. Number of Banks Used and Frequency

A further series of questions asked customers how many banks they used, and, with respect to their primary bank, how often they visited.

Number of Banks Used	% of Customers
Only One	15.3%
Two	35.3%
Three	28.9%
Four or More	20.5%

Frequency of Visits	% of Customers
Daily	2.1%
Twice Per Week	31.6%
Once Per Week	30.1%
2-4 Times Per Month	25.3%
Once Per Month or Less	10.9%

Travel Time to Primary Office	% of Customers
<5 Minutes	46.6%
>5 but <10 Minutes	31.2%
10-15 Minutes	11.6%
>15 Minutes	10.6%

5. Personal Investments

Another key question was: In which ways do you invest your money? The responses were as follows:

a) Real Estate

Almost 600 of the 900 (60%) respondents cited Real Estate with 405 (48%) stating it was their primary investment. It is not clear how many included their home in the definition of Real Estate as an investment but the assumption is that most people did.

b) Savings Accounts

Second only to Real Estate, Savings Accounts were listed 287 times (32.5%) as a primary investment, 175 times as a secondary investment and 154 times as the third investment.

c) Common Stocks

Far behind Real Estate and Savings Accounts, Common Stock was cited as the primary investment in only 187 cases, 148 times as the secondary investment and 141 times as the third most important investment.

d) Mutual Funds

Almost tied with Common Stocks were Mutual Funds with very similar responses.

e) Certificates of Deposit

Closely behind Mutual Funds were CDs with 157 cases of primary citation.

f) Other Investments

Bonds, Insurance and Collectables were well behind all of the other investment vehicles.

A final question in this area was: Which institution performs these investment services for you? The responses were:

Institution	% Customer Using
Stock Broker	45.5%
Savings & Loan	42.3%
Primary Bank	36.6%
Other Institution	29.2%
Bank other than Primary Bank	20.1%
Credit Union	13.8%

A key observation here is that while 45% of the respondents stated that they use a broker to handle their investments, stocks rated only third on the list of preferred investments and fewer than 5% of all respondents listed their broker as their primary financial institution.

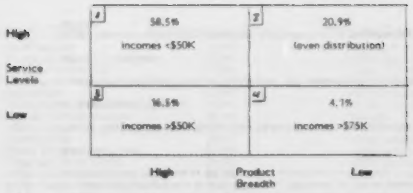
6. Financial Information Sources

The respondents were asked to list their principal source for information on banking services. The responses were as follows:

Information Source	% of Customers
Bank Statement Stuffers	43.3%
Newspaper Ads	15.9%
Friends	13.7%
Special Mail Fliers	12.3%
Lobby Displays	10.1%
Television	2.5%
Magazines	1.7%
Radio	0.4%
Billboards	0.1%

7. Customer Satisfaction Matrix

Finally, relative to the results to be reported in this article, customers were asked a series of questions pertaining to their perceived levels of satisfaction at their primary financial institution. The results of these questions have been combined into a matrix which reflects the satisfaction customers have with their primary bank relative to the perceptions they have as to the adequacy of the products and services currently provided. This matrix appears below and shows the income groups predominant in each quadrant.



What this matrix infers is that 6 out of 10 of these retail customers (Qd 1) perceive that their primary bank currently provides them with a sufficient array of products and services together with a high level of personal service. Further, proportionately more of the customers with annual income of less than $50K seem to share this feeling. Only a negligible number (4%) of all customers (Qd 4) feel that their bank fails to offer both a sufficient breadth of products and levels of personal service and attention. We also find higher incidences of this dissatisfaction among the most affluent customers who are more demanding in any event. In sum, 75% of all these retail customers perceive that their primary bank offers a broad enough range of products and services to meet their needs, while up to 80% of them feel that they are receiving satisfactory levels of personal attention from the bank. Thus, if this bank can be used in an exemplary manner, only 2 out of every 10 retail customers appear to be in need of something more in products and services, and these are most likely to be the most affluent customers.

Implications

The implications of these findings are manifold. It will take months to appreciate fully the conclusions to be drawn from the complete findings let alone the partial results reported here. However the principal implications are clear. First, that affluent retail bank customers have a variety of relationships with various institutions, and do not feel it is important for any one bank to provide them with what industry executives have been led to believe is "broad range of products and services". To the contrary, **these retail customers are basically satisfied with accurate, safe custodial services.** They want easy access to the cash they keep close to home through ATMs, extended hours and drive-ups; but, as a result of 50 years of government regulation, retail customers have been forced to build professional relationships with other individuals and entities such as CPAs and investment advisors. After so many generations of these kinds of relationships, it is now inconceivable to most people that a bank could suddenly gain equal expertise in these fields. For example, the thought of giving up their relationship with a CPA or Investment Advisor to allow their banker to take on those roles is beyond comprehension to these customers. All they really want from their bank is that their "custodian" provides safe keeping and book keeping services quickly, accurately and with some recognition for the customer's loyalty. Also, as presented in an earlier table, at an average, only 10% of all retail customers seemed interested in the "non-custodial" products and services".

A second major implication is that interest rates and product variety are not as important as the level of personalized service. **In reviewing four major interest bearing accounts, the respondents had no idea what interest rate they were being paid in over 65% of the cases,** while an additional 15-20% of the respondents stated that they were being paid a competitive rate when, in fact, they were not. This follows closely the findings of the matrix whereby customers receiving a lot of "High Touch" service perceived that the bank had a broad range of products and services when, in relationship to other very large banks, it does not. Throughout the survey, customers asked for more drive-ups, longer branch hours, more ATMs, and service with a smile, nothing more. As observed in previous studies conducted by the authors involving other banks, it appears that more and more retail customers are establishing financial relationships with in-house workplace facilities such as credit unions for their convenience and easy accessibility. In turn, especially large credit unions are responding to their patrons' needs by offering more banking products such as NOW accounts, personal lines of credit, short and long term investment instruments, travel services and prestige credit cards.

A principal finding of the Virginia study, one which was strongly supported in the West Coast research, is that customers are really not interested in their bank developing a broad array of new, technologically sophisticated products.[2] The reaction to Home Banking on the questionnaire was almost non-existent while the thought of bankers entering the Tax Preparation or Stock Investment Advisory fields met with outright skepticism. As it is, about one third of the products and services currently offered by typical community banks are not used in sufficient volume to justify their continued survival. The majority of retail bank customers feel that **the breadth of products and services currently offered**

is already wide and sufficient for the level of relationship they intend to have with their bank.

A third implication from these findings is that even among the most affluent, more and more marriages see both partners working, not only to increase life styles, but also to take advantage of and utilize newly affordable education levels. As a result, the concept of a "housewife" managing the accounts of the family and being someone "free" to come into the bank anytime between 10 am and 3 pm is worse than erroneous; it is down right archaic! The implication for retail bankers is straightforward. They must find a way to open the bank during those hours most convenient to their retail customers not just their merchant accounts. In other, recent non-related research, almost half of all surveyed consumers stated that their banks' hours were inconvenient. If retail bankers cannot resolve this issue, they will have even less interface with their key depositors and less and less opportunity to provide them with the "High Touch", personalized service levels that they really want. Further, as retail customer traffic in the branches dries up even more, the incremental costs of keeping any branch office open will increase exponentially. This general phenomenon is demonstrated by the fact that more than 44% of the customers surveyed use Bank-by-Mail even though over 65% of them live within 5 minutes drive of a branch office. Drive-up facilities, if they are open after hours, and ATMs on the weekends are the second most convenient means of bank interface. This, in turn, implies that retail bankers will never get to practice much of their newly developed sales skills on their busiest, most affluent customers as they seldom come into the bank. The research also implies that while these prime customers are exposed to a lot of promotions by various financial institutions on television and radio and in their morning newspaper, they either "tune out" or do not give such promotions sufficient credence to warrant detailed attention. Depositors focus strongly, however, on their monthly statement stuffers.

A fourth implication from the findings is that while the affluent may double in stocks and bonds, many retail customers, whether they earn $25,000 or $100,000 a year, perceive of their home and other real estate as their primary financial investment; their liquidity accounts at their primary bank and in their S&L their second most important asset; and, their stocks are merely third, quite a ways behind. Therefore, it is even more important that the fundamental custodial services for these deposits as provided by banks are delivered faultlessly and with some appreciation. For example, while a customer's $10,000 CD may not be very important to the bank in its overall scheme of things, it is probably the major

liquid investment of the family doing business with the bank. It is their savings which they have consigned to the bank for safe keeping. They want to place that deposit with a bank which sends off more signals which communicate the bank's pleasure at having the business.

Strategic Lessons

The strategic lessons from these findings are significant. Foremost might be the finding that product development, especially in the "High Tech" area, appears far less important, necessary or desired than the further enhancement of personalized service levels in the branches. This "message" from the research flies in the face of a broad array of strategic steps taken over the past few years by retail banks, many of which have consciously decreased the "High Touch" aspects of retail banking in lieu of "High Tech". Clearly a reassessment is needed along with more psychographics-based research.

A corollary to this finding is that such a high degree of adults are working in the mid-1980s that the traditional branch hours of 10 am to 3 pm serve only a minority of customers. Some new and highly creative solutions must be found if the relationship between retail banks and their best customers is not to be relegated to something akin to one's relationship with the telephone company. Whether this issue is best addressed by finding new ways to service customers in their homes or by finding cost-effective ways to open the branch offices during different hours, is yet to be determined.

A further strategic lesson would be that while the very largest retail banks may continue to perform "High Tech" product research and development, for most banks, even large regional banks, they will not have large enough segments of interested customers to justify adopting many of these latest concepts including Home Banking. It would appear to be headed for the same fate as retail truncation.

Finally, in the area of strategic lessons, one cannot escape the entire issue of credibility beyond a safe keeping relationship. While bankers have been quick to adopt a broad range of new services in a very short time, the marketplace appears nowhere near as quick to accept that these bankers know what they are doing in those areas just because they have adopted them. When it takes a major insurance enterprise such as CIGNA over 6 years to field an independent financial services sales force of over 1,000 while investing more than $50MM in the fee-based products to support that highly skilled sales organization,

retail bankers must realize that they cannot change their basic image with their customers from that of custodian to that of creative investment advisor in just a few short months or even years. It is a very large image gulf to span and may take a decade or more.

Marketing Lessons

The marketing lessons derived from the research are equally profound. As customers find less and less time to visit their branch and give less and less credence to media-delivered financial information, marketeers must rethink how they can best get their prime retail customers to heed what is taking place in their banks; and, how to get them to enter into a broader range of relationships through multiple accounts rather than feel any need to open different accounts at multiple institutions. Just what that message should be, what it should say and where and how it should be communicated is each individual banker's dilemma. The status quo, however, does not appear acceptable.

Also from a marketing standpoint, the entire premise fostered on the banking industry over the past five years that attempts to turn retail banks into merchandisers needs to be reformulated. It is apparent from the research that retail customers do not want their banks to be boutiques nor do they perceive of their bankers as able to successfully manage any form of giant financial supermarket. These bankers are only digging their holes deeper in any event as teller and CSR turnover continues high industry-wide and training costs attributable to more sophisticated products continue to rise. What customers want is something much more fundamental and akin to the basic relationship they had prior to deregulation with, perhaps, the one caveat that they get a market rate on their deposits, something that is theoretically related directly to cost reduction and, in turn, inversely related to offerings of unwanted boutique services. This is a further reason why retail banks will continue to face stronger competition from conveniently situated and accessible credit unions or even larger department store chain services from the likes of Sears or J.C. Penneys.

Next Steps

The next steps for retail bank management must include a broad-based array of programs to reorient the bank and the branch staff toward "High Touch" service levels. These programs might well include the centralization of all paperflows and functions not needed in the branches, including the automation of all manually developed branch reports,

to free up more time in those offices for customer directed attention. Only after these operational steps can sales training, telemarketing and other steps take place in a productive environment and with full staff support.

Further, branch hours must be revised to address prime retail customer convenience relevant to the demographics of work habits in the mid-to late-1980s. This would include extended hours at the drive-ups, more ATMs and ATMs with a greater variety of functions.

Finally, if bankers can remove the clerical work from the branches, then, perhaps they can remove the clerks, too, and begin staffing their branches, now open at the customer's convenience, with people more akin to service industry positions - former school teachers and airline personnel, for example. These are not the penultimate solutions, but rather the very early stages of a highly creative thought process spanning the next few years. And, oh yes, we would be remiss without adding, more research is needed!

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1. Gwin, John M. and John H. Lindgren, Jr., "Bank Attribute Determinance: Initial Findings in the Consumer Choice Process", University of Virginia, Unpublished Research Paper.

2. Forbes; "Can the Performance Match the Promise?", January 27, 1986.

3. Wall Street Journal; "Bankers Hours", February 14, 1986.

Senator GORTON. Senator Garn.

OPENING STATEMENT OF SENATOR GARN

Senator GARN. Thank you, Mr. Chairman.

First of all, let me thank you, Senator Gorton, for holding these hearings. As you outlined, they are to cover a particular area that we have not covered in depth.

Second, I would like to say I'm a little bit surprised by the comments of my distinguished friend and colleague from Wisconsin about hearings that are stacked. Over the last 5 years since I have been chairman of the full committee, we have held more hearings on these issues and heard more witnesses than in any other period in the history of this committee. Almost ad nauseam.

Many of the issues are not new issues. They were issues that existed prior to me even becoming a Senator, let alone chairman of the committee. Yet, nevertheless, I have sat untold hours in that chair with a widening bottom and a receding hairline as a result of that for years listening to testimony from anyone who wished to testify on any side of an issue. Whatever the issues are, that policy has not been changed and it will not be changed in the future. Whatever the witness list is today, if people want more hearings and they want somebody invited, they will be heard and I will be here to hear them.

So whatever differences of opinion we may have substantively or the direction, these hearings are not stacked and people have been given an opportunity to be heard in the past, in the present, and they will be in the future. And I think it is important to hear all sides of an issue. We certainly have heard the negative over the last 5 years. We have certainly heard all of those who have their heads stuck in the sand and who refuse to recognize that the world rather dramatically changes out there, changes that are occurring rapidly in the marketplace, whether we do anything about it in this committee or in Congress or not. We have been derelict in our duties. It has been nearly 4 years since we have had any substantive legislation out of the Congress of the United States, but in those 4 years, boy, has the marketplace changed.

Now, yes, I think it's time we move ahead and I think it's time we make some decisions and I intend to do that as rapidly as possible. Regardless of the desires of this committee, regardless of the desires of the Senate or the House, this Senator will try to push for comprehensive legislation and we will continue to hear witnesses of all sides of issues regardless of how boring they may be.

Thank you, Mr. Chairman.

Senator GORTON. I wish the chairman of the committee would make himself clear.

Senator GARN. I don't want to take any more time or I would. [Laughter.]

Senator GORTON. Senator Hecht.

Senator HECHT. Thank you, Mr. Chairman. There's nothing I could add to that.

Senator GORTON. Mr. Kehrer, we will start with you and we would appreciate our witnesses limiting their remarks to 10 minutes. Their written statements will be included in the record and I

suspect all of them will have a number of questions which members will ask of them.

STATEMENT OF KENNETH KEHRER, CONSULTANT AND RESEARCHER, KENNETH KEHRER ASSOCIATES, NEW JERSEY

Mr. KEHRER. Thank you. I am Kenneth Kehrer. I am an independent consultant based in Princeton, NJ, and I've done extensive research on consumer attitudes toward banking, financial services, deregulation, and research on how various institutions are responding to these consumer needs by offering a wider range of financial services.

CONSUMERS WANT TO CONSOLIDATE FINANCIAL SERVICES

Today I will present strong evidence that the majority of Americans want to consolidate their financial services. They want to be able to buy such financial services as insurance, securities, and residential real estate brokerage where they bank.

This evidence is based upon my independent research on the Survey of Consumer Finance. This is a large-scale survey of a national sample of 5,000 households. In-person interviews for this survey were conducted in 1983 by the Federal Reserve Board, the Comptroller of the Currency, and other Federal agencies.

The survey provides a comprehensive look at how American families use financial services and their wants and needs. By virtue of its size, comprehensiveness and the quality of the data, the Survey of Consumer Finance is unquestionably the best source of information about consumer interest in expanding the services that banks can offer.

I have some exhibits here that will help to illustrate my presentation.

Exhibit 1 indicates that the overwhelming majority of Americans want to consolidate their financial services business in one place. Almost two-thirds consider consolidation important and 4 out of 10 say that consolidation is so important that they will choose where they bank or conduct their financial business based upon whether or not the institutions in their area offer a broader range of financial services.

Along with the actions of this committee and the committee on the other side, the desire to consolidate is probably the single most important force shaping the emerging financial services industry.

Now interest in consolidation is high all across the country. It's highest in the north central Midwest region where two-thirds express interest in consolidation, but it's also high in the Northeast and South. It's somewhat lower in the Western States but there still the majority still favors consolidation.

Interest in consolidating financial services is high in every type of community, in rural areas, in the suburbs, in central cities. It's lowest in the central cities of the 12 largest metropolitan areas, but even there more than 4 out of 10 favor the opportunity to consolidate.

This interest in consolidation, in consolidating one's financial business, is very widespread. The desire to consolidate is felt in all walks of life, across all occupations. Consolidation is sought by the

rich as well as the poor, although it is most popular among middle-income families where more than half say that consolidation is so important that they will choose where they bank or conduct their financial business based upon the opportunity to consolidate.

Now the survey supports one of Senator Proxmire's arguments this morning that the Americans who want to consolidate are just like other American families in that they prefer overwhelmingly to do business with their local banks and thrifts.

Here we're comparing what I call the consolidation households—that is, the 4 out of 10 who strongly prefer to consolidate—with all other American households. As you can see, Americans prefer local financial institutions 3-to-1 over national organizations such as Sears and Beneficial who we will hear from later this morning.

They also prefer local institutions, local banks, and thrifts, over statewide or regional organizations by a 3-to-1 margin.

But consumers' needs are being frustrated because banks cannot offer some of the services that these national organizations can.

How consolidated are these households already? Are they just talking about consolidation? Do they just say they are interested in a survey but are not doing anything about it, or are they actually consolidating already?

Exhibit 5 indicates that households that most want to consolidate their financial services are already doing business with fewer commercial banks, savings and loans, and finance companies. They do business with one less commercial bank than other households, one less savings and loan, one less finance company per household. So the households that most want to consolidate have already cut back on the number of financial institutions they use and they are taking some of this business to the diversified financial services organizations, even though they would prefer to take this business to their bank.

Another aspect of consolidation is the number of relationships a consumer has with a provider. What is the extent of consolidation of account relationships with one's main bank?

Compared with other households, the households that feel opportunities to consolidate are very important or somewhat important are many, many times more likely to have additional relationships with their bank. These consolidation households are seven times more likely to have an additional checking account or IRA with their bank. They are six times more likely to have a savings certificate, a money market account, or a bank card where they bank. They are 10 times more likely than other households to have a mortgage with their main bank. They are nine times more likely to have a loan with their main bank. Notice, however, that they are not much more likely to have a brokerage account.

Thus, the households that want to consolidate have already achieved substantial consolidation with their bank and they want more. They say they want more, but they can't get some of these services now.

[The charts submitted by Mr. Kehrer follow:]

EXHIBIT 1

ORIENTATION TOWARD CONSOLIDATING FINANCIAL SERVICES

	PERCENT OF HOUSEHOLDS
VERY IMPORTANT	41
SOMEWHAT IMPORTANT	22
NOT VERY IMPORTANT	11
NOT IMPORTANT AT ALL	26
TOTAL	100

*Kenneth Kehrer

EXHIBIT 2

REGIONAL DIFFERENCES IN ORIENTATION TOWARD CONSOLIDATION (PERCENT OF HOUSEHOLDS)

	VERY IMPORTANT	SOMEWHAT IMPORTANT	TOTAL
NORTHEAST	41	21	62
NORTH CENTRAL	43	24	67
SOUTH	40	20	60
WEST	38	18	56

✱Kenneth Kehrer

EXHIBIT 3

DIFFERENCES IN ORIENTATION TOWARD CONSOLIDATION BY TYPE OF PLACE (PERCENT OF HOUSEHOLDS)

	VERY IMPORTANT	SOMEWHAT IMPORTANT	TOTAL
CENTRAL CITIES OF 12 LARGEST METRO AREAS	26	17	43
CENTRAL CITIES OF OTHER SMSAs	43	21	64
SUBURBS OF 12 LARGEST METRO AREAS	37	27	64
SUBURBS OF OTHER SMSAs	43	23	66
ADJACENT AREAS	45	21	66
OUTLYING/RURAL AREAS	42	22	64

*Kenneth Kehrer

EXHIBIT 4

PREFERENCES FOR TYPE OF FINANCIAL SERVICES ORGANIZATION (PERCENT OF HOUSEHOLDS)

	CONSOLIDATION HOUSEHOLDS	OTHER HOUSEHOLDS
NATIONWIDE FINANCIAL SERVICES ORGANIZATION	19	19
STATEWIDE BANK OR THRIFT	18	15
LOCAL BANK OR THRIFT	61	59
NO PREFERENCE	2	7
TOTAL	100	100

✱Kenneth Kehrer

EXHIBIT 5

NUMBER OF FINANCIAL INSTITUTIONS THAT HOUSEHOLDS DO BUSINESS WITH

	CONSOLIDATION HOUSEHOLDS	OTHER HOUSEHOLDS
COMMERCIAL BANKS	1.8	2.7
S & Ls	1.7	2.8
FINANCE COMPANIES	1.5	2.6

✱Kenneth Kehrer

EXHIBIT 6

EXTENT OF CURRENT CONSOLIDATION: ADDITIONAL RELATIONSHIPS WITH MAIN BANK (PERCENT OF HOUSEHOLDS)

	VERY IMPORTANT	SOMEWHAT IMPORTANT	NOT IMPORTAN
ANOTHER CHECKING ACCOUNT	13	14	2
IRA	7	7	1
SAVING CERTIFICATE	18	14	3
MONEY MARKET OR OTHER SAVINGS ACCOUNT	37	31	6
BANK CARD	23	21	4
MORTGAGE	10	9	1
LOAN	18	13	2
BROKERAGE OR TRUST ACCOUNT	2	1	1

*Kenneth Kehrer

EXHIBIT 7

ORIENTATION TOWARD FINANCIAL INSTITUTIONS FOR NON-TRADITIONAL PRODUCTS (PERCENT OF HOUSEHOLDS INTERESTED)

	CONSOLIDATION HOUSEHOLDS	OTHER HOUSEHOLDS
SECURITIES	17	7
LIFE INSURANCE	14	8
PROPERTY/CASUALTY INSURANCE	17	10
RESIDENTIAL REAL ESTATE BROKERAGE	18	10

Kenneth Kehrer

ADDITIONAL SERVICES DESIRED BY CONSUMERS

Mr. KEHRER. Well, what kinds of additional services would Americans like to be able to purchase where they bank? The Survey of Consumer Finance asked about four: securities, life insurance, property/casualty insurance, and residential real estate brokerage services.

Now, 17 percent of all consolidation households say they would like to buy securities where they bank; 14 percent are interested in buying life insurance and annuities where they bank; 17 percent say they are interested in buying their automobile and homeowners coverage where they bank; and 18 percent say they are interested in buying and selling their home where they bank.

In general, notice that the households that most want to consolidate are about twice as likely to want these kinds of broader services where they bank than other households.

In conclusion, I believe that the information I have shown you this morning demonstrates that interest in consolidating one's financial business is both very strong and widespread and that this desire is being frustrated because banks are prohibited from offering certain services.

Thank you.

Senator GORTON. Thank you, Mr. Kehrer. That's a most interesting presentation. It's obviously radically different from the Metzger-Day study which Senator Proxmire referred to or, for that matter, the second one to which he referred, in which the conclusion was that people want better services, not new products or services.

Are there differences? Are they both valid because they ask different questions? Or how do you reconcile the two sets of attitudes?

Mr. KEHRER. I have not seen the study to which the Senator referred. I have read his comment in the record about the study and that's the extent of my knowledge of it. From that comment, I would say the studies are looking at different populations. The study to which he refers is a study, as I understand it, of a particular bank's customers, a particular bank's retail customers. That bank tends to have fairly high income customers. I believe the record indicates that the average household income is over $60,000 for its customers. And that study is probably a perfectly valid expression of how those customers feel.

However, the survey on which I base my research is a national representative sample beyond dispute in terms of the quality of the information, having been supervised by the technical staff of the Federal Reserve Board.

Senator GORTON. I'm sorry?

Mr. KEHRER. My study was conducted through the Federal Reserve Board and supervised by their technical staff.

Senator GORTON. Who actually conducted it?

Mr. KEHRER. The actual survey was commissioned and administered by the Federal Reserve Board. My study was an independent study using that publicly available data base.

Senator GORTON. As you heard from my opening statement, the Stanford Research Institute was going to testify today but couldn't clear its testimony on time. That institute did the research for and

designed the cash management account of the late 1970's which obviously filled the void for a service which financial institutions were not before that time providing to their customers.

What do you think the next step or major product in the financial services arena is likely to be?

Mr. KEHRER. The kinds of products the consumers seem to want are additional ways of managing their personal finances through their bank and the kinds of products that seem to be attractive to consumers are those that provide them the ability to do that kind of management more easily. For example, unified statements, the ability to automatically pay bills, the ability to switch funds from one account to another, the ability to save and invest as well as to do transactions where they bank.

Senator GORTON. You have already indicated, of course, that people are moving in the direction of one-stop shopping as it is. In order for them to reach those goals, are structural changes in banking needed or does your study or your interpretation simply indicate that people can reach that goal with the present decentralized nature of financial services offered?

INSURANCE AND INVESTMENT NEEDS

Mr. KEHRER. Consumers are clearly using additional banking services where they bank. They are interested in buying insurance products, meeting their insurance needs their other kinds of investment needs. Insurance policies are a useful example of consumers being frustrated where they bank. They have to take that business elsewhere.

The ability to merge one's credit needs with one's savings and investment needs is something that I think is felt by consumers and they are frustrated by that separation.

Senator GORTON. So it's your view that consumers want banks to be able to provide a wide range of services that they are legally prohibited from providing at the present time?

Mr. KEHRER. That's right, and my research also indicates, as Senator Proxmire indicated earlier, that Americans really turn to their banker for financial advice but bankers are prohibited from giving certain kinds of financial advice; for example, the advice about securities investments; and yet consumers are very clearly interested. They look to their banker for that advice, but right now the bankers' hands are tied.

Senator GORTON. Everything you testified to related to consumer attitudes, what consumers would like to have, what they are in fact already doing.

Did your research examine the attitudes of bank customers on subjects which are normally considered to be consumer interest subjects? For example, credit card interest rates, check hold policies, fees for returned checks and the like. Do you have any information or insight on consumer attitudes toward those questions?

Mr. KEHRER. Yes; surprising to me, given a lot of the information around about concern over bank fees and the increase in bank fees in recent years and so on, I found in studying this data base that consumers tend to regard fees as less important than other things. They tend to believe that convenience is the most important crite-

rion in choosing where they bank. They will tend to put the convenience factor 4 to 1 over such things as fees. They will tend to look at opportunities to consolidate. They are twice as likely to feel that opportunities to consolidate are most important when choosing a bank than fees.

Indeed, my research seems to indicate that consumers don't shy away from fees. They are willing to pay for value and value to them is the ability to manage their finances, manage their credit needs, their savings and investments in one institution. They are willing to pay a reasonable fee for that, a fair fee for that.

Senator GORTON. Does that mean that consumers would be very concerned about check hold policies? You're not telling me that they are indifferent to how long a check is held before it's credited to their account, are you?

Mr. KEHRER. My research did not touch on that issue so I can't comment on it.

Senator GORTON. You can't comment on it?

Mr. KEHRER. No.

Senator GORTON. You haven't commented on it inferentially by saying that people are concerned with convenience and service? You don't imagine that people would be indifferent to those policies, do you?

Mr. KEHRER. That would be speculation on my part. My research did not directly shed light on that. It can shed light on dollar fees and with respect to that consumers do not seem to feel that dollar fees are that important in their banking. They will choose to place their financial business with an institution that offers them good service, that offers them the ability to manage their affairs in one place, and are willing to pay fees for that.

Senator GORTON. Now if Congress were to allow the evolution of financial services market, is there any particular segment or any particular company, for that matter, that will gain a substantial marketing advantage over its competitors? That is to say, banks as against thrifts, as against insurance companies or retailers like Sears?

Mr. KEHRER. I see no one institution that has an advantage in this marketplace under those conditions. I see banks and thrifts having a significant advantage in that they have customer loyalty. The customer looks to them for their financial affairs. Consumers prefer to do business with them.

On the other hand, the insurance companies and securities companies and mutual funds companies—those organizations have products that the consumers want that banks and thrifts currently do not have. They have experience in servicing those products and consequently they have a countervailing advantage, if you will, in the marketplace. In fact, I see many benefits to the consumer of marrying those kinds of benefits, marrying the customer service tradition of banks and thrifts with the product experience and product service experience of the securities firms, the mutual funds companies, and the insurance companies in providing better products and service to consumers.

Senator GORTON. Senator Proxmire.

Senator PROXMIRE. Thank you, Mr. Chairman.

I'm puzzled, Mr. Kehrer. In the first place, we didn't see your testimony at all. Do you have a written statement?

Mr. KEHRER. I will supply that to the committee.

Senator PROXMIRE. Well, you see, if we don't get it in advance it's very hard for us to have an opportunity to study it and to prepare questions on it and it's unusual. Usually we require witnesses to supply a written statement in advance. We make some exceptions for top officials who can't do it, but in this case it seems to me that we ought to have it.

[The complete prepared statement which was subsequently submitted for the record follows:]

STATEMENT OF
KENNETH KEHRER, Ph.D.
PRINCIPAL
KENNETH KEHRER ASSOCIATES

BEFORE THE
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE

Overnight Hearings On
THE DRIVING FORCES BEHIND, AND CONSUMER BENEFITS ASSOCIATED WITH,
THE CHANGING FINANCIAL SERVICES ENVIRONMENT

May 7, 1986

I am an independent consultant based in Princeton, New Jersey. I have done extensive research on

- consumer attitudes toward banking, financial services, and deregulation, and
- how various institutions are responding to these consumer needs by offering a broader range of financial services.

Today I will present strong evidence that the majority of Americans want to consolidate their financial affairs and that large numbers of consumers want to be able to buy such financial services as insurance, securities and residential real estate brokerage services where they bank.

This evidence is based on my research on the Survey of Consumer Finance, a large-scale survey of a representative national sample of 5,000 households. This survey was conducted in 1983 by the Federal Reserve Board, the Comptroller of the Currency, and other participating federal agencies. Over 75 percent of the sample completed lengthy, in-person interviews administered by the Survey Research Center of the University of Michigan. This Fed Survey provides a comprehensive examination of how American families use financial services and their wants and needs. By virtue of its size and the comprehensiveness and quality of the data, the Survey of Consumer Finance is unquestionably the best source of information about consumer interest in expanding the services that banks can offer.

From this survey, it is clear that the overwhelming majority of Americans want to consolidate their financial services (Exhibit 1). Almost two-thirds of all American households feel that it is important to them to be able to obtain many financial services at one place. And four-out-of-ten say that opportunities to consolidate are very important -- so important that it is a primary reason for choosing where they bank or obtain financial services. Along with the deregulation steps take by Congress, the desire to consolidate one's financial affairs is the most important force in the emerging consumer financial services industry.

Interest in consolidation is high all across the country (Exhibit 2). It is highest in the North Central, Midwest region, where fully two-thirds

of all households express interest in consolidation. Six-out-of-ten households in the Northeast and South feel that consolidation is important to them. Interest is somewhat lower in the Western states, but even there the majority prefers to bank where they have a broad range of financial services.

Interest in consolidating financial services is high in every type of community — rural areas, the suburbs, and central cities (Exhibit 3). Interest is lowest in the central cities of the 12 largest metropolitan areas, but even there more than four-out-of-ten households feel that opportunities to consolidate are important.

This interest in being able to obtain a broad range of financial services where one banks is very widespread. The desire to consolidate is felt in all walks of life — by the rich as well as the poor. However, interest in consolidation is most popular among middle-income families.

The majority of those households (where the head is under age 55 and household income is between $20,000 and $70,000 a year) say that consolidation is very important to them. And almost nine-out-of-ten of these middle-income households express some interest in a broad range of services where they bank.

Where Do Americans Want to Conduct Their Financial Business?

The households that most want to consolidate are just like other American households: they overwhelmingly prefer to do business with local banks and thrifts. In Exhibit 4, I compare what I call "consolidation households" (i.e., the one-out-of-four U.S. households who most want to consolidate) with all other households (i.e., the two-in-ten who say consolidation is somewhat important but not very important, plus the four-in-ten who are not interested in consolidating). Like other American households, the households that most want to consolidate prefer local financial institutions 3:1 over either

- national financial services organizations such as the national retailers, insurance companies, securities brokerage firms, and finance companies, or
- statewide or regional institutions.

But these consumers are being frustrated because their community bank cannot offer some of the services they want.

How Much Consolidation Has Already Taken Place?

The households that most want to consolidate have already achieved substantial consolidation in the number of institutions they do business with. On average, these "consolidation households" do business with one less commercial bank, one less S&L, and one less finance company (Exhibit 5).

Thus the households that want a broader range of financial services in one place have already cut back on the number of financial institutions they use (i.e., "institution consolidation"). Undoubtedly, they are taking some of this business to the national diversified financial services organizations such as Sears and Beneficial, even though they would prefer to take this business to their local bank.

Another aspect of consolidation is the number of relationships a consumer has with one provider. In Exhibit 6, I examine the extent of this "relationship consolidation" with one's main bank. The households that want to consolidate are many, many times more likely than other households to have additional relationships with their main bank. The households who say that having a broad range of services where they bank is very important are

- six time more likely to have a savings certificate, money market account, or bank card at their main bank,
- seven times more likely to have another checking account or IRA at that bank,
- nine times more likely to have a loan there, and
- ten times more likely to have a mortgage at their main bank.

The households who say that opportunities to consolidate are somewhat important are also many times more likely to have multiple relationships with their main bank than households who feel consolidation is not important, but not as likely as the "consolidation households."

Thus, American households are not just talking to survey takers about consolidating, they are voting with their checkbooks and savings. The majority have already achieved both substantial institutional consolidation and dramatic relationship consolidation. And they say they want more!

What Kinds of Additional Financial Services Do They Want Where They Bank?

The Survey of Consumer Finance asked Americans about their interest in having their bank offer four kinds of non-traditional services:

- buying and selling market stocks and bonds for its customers
- selling life insurance
- selling home and automobile insurance
- helping customers find buyers or sellers for homes and other properties as real estate agents

A significant number of households expressed interest in these specific services. Based on the Survey of Consumer Finance, 8.9 million households are interested in securities brokerage where they bank, 8.4 million are interested in life insurance, 10.3 million in property/casualty insurance, and 10.6 million are interested in having banks provide residential real estate brokerage services.

Of course, the households who are most interested in consolidating were much more interested in having each of these services available where they bank than other households. Seventeen percent of the consolidation households were interested in either trading securities or buying personal property/casualty insurance where they bank, 14 percent were interested in life insurance, and 18 percent were interested in banks providing residential real estate brokerage services (Exhibit 7). In general, the households that most want a broad range of financial services provided by banks are about twice as likely as other households to want banks to offer these particular non-traditional services.

Conclusion

In conclusion, I believe that the information I have shown you this morning demonstrates that interest in consolidating one's financial business in one institution is both very strong and very widespread. Moreover, the desire of Americans to consolidate their financial business at their bank is being frustrated, because most banks are prohibited from offering such services as securities, insurance and real estate brokerage.

Senator PROXMIRE. I'm mystified also by this kind of a study. You say you are a consultant and researcher but you didn't conduct any of these polls. These were all taken from the Federal Reserve and other bank regulators?

Mr. KEHRER. This was a national survey commissioned by the Federal Reserve, the Office of the Comptroller, and other participating agencies.

FED TAKES AN ENTIRELY DIFFERENT POSITION

Senator PROXMIRE. How do you explain the fact that the Federal Reserve takes an entirely different position than you appear to take here? They want to close the nonbank bank loophole. They think that's very important. They put it as a high priority. They have all this information available. You say they commissioned it. Yet they come to quite a different conclusion.

How do you arrive at that? Do you think there's something corrupt here by the Federal Reserve?

Mr. KEHRER. No; they may not have looked at this issue.

Senator PROXMIRE. They commissioned it, they conducted it, and they didn't even know about it?

Mr. KEHRER. Well, the survey was conducted primarily for the purpose of measuring the sources and distribution of wealth and debt in the country. The survey can also be used as a very valuable data base for a wide variety of purposes. I am not sure whether they have addressed this particular question in that data base.

I did. I did it for my own independent purposes and these are the results I found.

Senator PROXMIRE. Well, don't you think we ought to have the Federal Reserve give us their opinion? They have given their general opinion on nonbank banks. It's been very emphatic, very consistent, and they want us to close that loophole. Isn't that right?

Now you argue that many consumers want their financial services consolidated. I suppose it depends—in all these areas it depends so much on how the question is framed, how it's asked, as you know as a professional. You can get almost any answer you want from a consumer depending on how you ask it. I suppose if somebody came up to me and said, "Would you like to have a convenient situation where you could buy everything in one spot?" You'd say, "Sure, why not."

On the other hand, you say that consumers want to do business with their own local community bank. Now if they knew that their own local community bank would lose much of the resources they have available to provide loans to local businesses and you framed that into the question so they understood that, and they had the choice of having a place where they could have all their services consolidated on the one hand or have their local banks lose much of their resources on the other, they might give a different answer, might they not?

Mr. KEHRER. If that was the way the question was posed, they probably would give a different answer.

Senator PROXMIRE. Well, why wouldn't that be a kind of a situation that would realistically result?

Mr. KEHRER. I think that any result of any survey needs to be treated with some skepticism because of the kinds of issues you've raised.

However, I think that strong support for this survey comes from the fact that the very people who say they most want to consolidate are already consolidating—they're not just answering a survey question willy-nilly based upon how it's asked. In fact, the people who say that consolidation is very important—look at exhibit VI—13 to 2, people who say they want to consolidate are more likely to be consolidated already.

SOME 5,000 HOUSEHOLDS SURVEYED

Senator PROXMIRE. How many people are there? Are there 15 people who testified, who responded?

Mr. KEHRER. 5,000; this is a national sample of 5,000 households, nationally representative. The survey was conducted by the prestigious Survey Research Center at the University of Michigan. This survey is unquestionably the finest data base around to be able to answer these kinds of questions.

Senator PROXMIRE. Well, you account for the difference between your findings and the findings of the two studies that I submitted in my opening statement—and I have both of them right here—on the grounds that affluent customers would have a different view than the rank and file customers. It seems to me if there's any group who would be more interested in a variety of services it would be affluent customers. After all, they buy stocks and bonds and they have all kinds of interest in a variety of services. And yet the response both in the East and the West and on both coasts was very clear and very emphatic, that they were not interested in having their bank do all these additional services. Why?

Mr. KEHRER. Well, again, I have not been able to review those studies. The only thing I was speculating on was the fact that they were based on—one survey you referred to in the record was based upon a customer survey of a particular bank with relatively high income customers.

My research has found that the portion of Americans that are most interested in consolidating are middle Americans, middle-income households, although there's still strong interest among high-income and among low-income households.

I would also point out that this survey is a very large scale survey, 5,000 households, vis-a-vis the 900 households that you mentioned in your statement in the record. But nonetheless, I wouldn't think that would make a major difference. I would expect the 900 households to provide reasonable information.

Senator PROXMIRE. Finally, I want to return to the original question I asked. You can't think of any particular reason why the Federal Reserve, which as you say gathered this material, should not take the same position you take with respect to nonbank banks and the availability of so-called family banks, except that they didn't know the score; they didn't know what was going on; they didn't have the information. Is that right?

Mr. KEHRER. I think that they may not have looked at this particular aspect of the survey, which is a very large data base. To the

best of my knowledge, I'm the first one to have looked at those particular survey questions in this light.

Senator PROXMIRE. Thank you, Mr. Chairman.

Senator GORTON. Senator Garn is next but Senator D'Amato has come. Do you have an opening statement or a statement you would like to make?

Senator D'AMATO. Mr. Chairman, I have a statement that I would like read.

Senator GORTON. Without objection.

Senator D'AMATO. Thank you, Mr. Chairman.

STATEMENT OF SENATOR ALFONSE M. D'AMATO

I commend the chairman for holding these hearings regarding the potential benefits that consumers of financial services may realize as this market evolves. At the outset, let me state that I am wholeheartedly behind the idea of allowing consumers to participate in the financial marketplace. The return of the individual investor to the equity markets in recent months has helped fuel the expansion of these markets that has driven the stock market to all time highs.

While I am encouraged by the renewed participation of the individual investor in the equities markets, as chairman of the Securities Subcommittee I am concerned about the safety and soundness of the financial markets as well as the protection of the individual investor.

I think these issues should be of paramount concern to the members of this committee and to those who appear before it today. While I agree that competition in the financial marketplace is healthy, I also believe that such competition need not occur at the expense of investor protection or the soundness of our financial markets. While consumer convenience may be desired, I cannot comprehend how consumers will benefit from tearing down the barriers between commercial and investment banking erected by the Glass Steagall Act. It seems that the current legal structure, with some minor modifications, has served consumers fairly well over the last 50 years. I do not understand how consumers can benefit from the grant of authority to commercial banking institutions that would permit them to engage in the underwriting of mutual funds, mortgage-backed securities, commerical papers, and revenue bonds.

It is my studied opinion that permitting commercial banks to engage in these underwriting activities would benefit a handful of commercial banks, and not the consumers, and potentially sacrifice a safe and sound financial system. At present, consumers have many options regarding the choice of financial services. The destruction of the barrier between commercial and investment banking in the name of offering more options to the consumer is a ruse. The consumer is already confronted with a myriad of financial products; in fact, more than they know how to employ effectively. I believe that the expansion of financial services within the boundaries of safety and soundness concerns is a laudable goal and yet I'm not willing at this time to redefine the role of commercial

banking activities. I believe that the consumer wants better service from commercial banks and not more services.

Commercial banks and thrift institutions should concentrate on what they supposedly do best, extending credit. Therefore, they should concern themselves with offering a variety of investment opportunities or financial services to consumers only after they have mastered the extension of credit. Recent history has demonstrated through record numbers of bank and thrift failures that a refinement of skills in the credit extension area is definitely needed. However, if the banks and thrifts are truly concerned about the welfare of the consumer why don't they lower credit card interest rates and permit the consumer to have more income to invest in other financial products.

I look forward to the testimony of this morning's witnesses.

Senator GORTON. Thank you, Senator D'Amato. Senator Garn.

Senator GARN. Mr. Kehrer, I don't see any real conflict between what you're saying and what the Fed is saying. Senator Proxmire is correct on the Fed's position as far as the nonbank bank loophole. The Fed has also endorsed insurance brokerage, real estate brokerage, limited securities powers for banks.

You have a broad data base and I assume that there are a lot of other things you could take from that data base and come to other conclusions. So the Fed is correct. You are correct. It depends on what you want to take from that data.

So I don't see a conflict between what Senator Proxmire is saying and what you are saying on that particular issue.

From your research, though, do you think the changes in the financial services industry are consumer driven or are they driven by the services and products that are offered?

As an example, I don't know that anybody was out there demanding cash management account [CMA's] but once CMA's were available they were certainly very popular. So do you make any conclusion whether people are demanding these or when they're made available they think, "Hey, that's a nice idea," and they're in favor of it?

Mr. KEHRER. I think it's useful to differentiate between a general consumer need and the particular way that financial services organizations conceive how to meet that need. The CMA is an example of meeting a consolidation need. Individuals were interested in being able to manage resources and savings and investment in one account. The CMA was an example of how to do that.

Other kinds of vehicles or instruments are being developed and have been developed to meet those kind of needs.

Senator GARN. I have no further questions.

Senator GORTON. Senator Hecht.

Senator HECHT. Thank you, Mr. Chairman. I'm on a fast timeframe too, another committee, and I would like to forego my questions and hear the next panel.

Senator GORTON. Mr. Kehrer, thank you very much for being here. You are going to submit your materials in writing?

Mr. KEHRER. Yes, I will.

[Information requested was not received in time of publication.]

Senator GORTON. Thank you. We would appreciate having it.

Now we have a panel of Mr. Wood and Mr. Heller. Mr. Wood, we'd be happy to start with you.

STATEMENT OF ROBERT E. WOOD II, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, CONSUMER BANKING DIVISION, DEAN WITTER FINANCIAL SERVICES GROUP, SEARS CORP.

Mr. WOOD. I am Robert Wood, chairman of the consumer banking division of Dean Witter, a unit of Sears, Roebuck & Co.

Mr. Chairman and members of this distinguished subcommittee: I will summarize a portion of my written statement and ask that the full text of the statement be made part of the record.

Senator GORTON. It will be included.

Mr. WOOD. It is with great pleasure that I appear here today to discuss what benefits the future holds for consumers of financial services.

To ensure that the growth and innovation of the industry can proceed along logical and, indeed, healthy lines, Mr. Chairman, Sears believes this committee should proceed with legislation. That legislation should allow institutions the greatest amount of flexibility to meet the needs of their customers while, at the same time, giving regulators the tools necessary to deal with a dynamic financial service environment.

BENEFITS TO CONSUMERS

Having said that, let me turn to the issue before this subcommittee which is how consumers benefit from a competitive financial services marketplace. In doing so, I would like to cover three areas: first, that the starting point of the subcommittee's deliberations should be the needs of consumers in the financial service industry; second, the concept of one-stop shopping as one approach to delivering financial service products to consumers; and, finally, new approaches to the delivery of financial services.

Mr. Chairman, as the issue of these hearings indicates, we believe that the starting point for consideration is always the consumer. We also understand that consumers are not knocking on doors on Capitol Hill to be heard on the issue of the future of the financial services industry. Consumers generally buy solutions, not things. That's the wisdom in the old marketing maxim explaining why people buy quarter-inch drill bits. They really don't want quarter-inch drill bits. What they want is quarter-inch holes.

That is as true in financial services as it is in the hardware business. The consumer wants solutions, not particular institutions. Consumers do not want stock brokers, banks, or insurance companies. They want effective delivery systems for financial services. They want their financial affairs handled efficiently and professionally with full assurance of security. Consumers want all of those qualities offered at a convenient, accessible place. Once those of us in the financial services business understand those needs and meet them, the consumer benefits. In that process, businesses and ultimately the economy benefit as well.

Our market research regarding consumer preferences confirms these statements. Several surveys of consumer responses that Sears has undertaken over the years revealed these consumer prefer-

ences: 71 percent said that a central location to handle all consumer transaction needs was a good idea; and responses included comments about liking the one-stop shopping idea as well as time and fuel savings.

The second point that I would like to discuss—the concept of one-stop shopping—proceeds from those studies and market research.

There is a desire on the part of consumers to conduct their financial transactions with the convenience afforded by one-stop shopping. That is not to say that all consumers prefer one-stop shopping. Instead, Sears believes there is a large segment of the population which has not established relationships with traditional providers of financial services in their traditional places of business and who would prefer the convenience of one-stop shopping.

By way of illustration, attached to my testimony are three charts which single out the conditions in the securities brokerage industry as of 1980. These charts demonstrate the relationship between all U.S. households, brokerage customers, and Sears customers by level of household income. Essentially, the figures represented in the charts demonstrate that while the traditional providers of securities brokerage services did an excellent job of marketing to consumers in the top 20-percent income brackets, there was a large part of the population, the middle market, which was largely untouched. That market is the traditional Sears market.

SEARS ENTRY INTO THE SECURITIES INDUSTRY

This information, as well as other considerations, formed the basis for our entry into the securities industry in order to serve this large segment of the securities market. We subsequently put together our version of one-stop shopping—offices of Dean Witter, Coldwell Banker, Allstate, and in California, Sears Savings Bank in one location in each of 313 Sears stores. Our experience with those Sears financial centers, created in response to a need and a market, has been very good.

Bearing in mind the charts reviewed earlier in my testimony, let me review Dean Witter's experience in the financial centers as the securities brokerage part of the operation.

Also, 35 to 40 percent of Dean Witter's new accounts are opened through those centers today. Now, 80 percent of these accounts are either first-time brokerage accounts or reactivated accounts representing new capital to the industry.

These statistics overall show that Sears targeting of a large untapped segment of the securities market, combined with the convenience and accessibility of the Sears financial centers, was very effective.

Over two-thirds of these customers had stocks in their portfolios.

And 8 of 10 visitors to Sears financial centers said that Sears has done an excellent job of bringing together financial services in one place.

Finally, in 1985 alone, Dean Witter opened over 200,000 accounts through this system, as opposed to 154,000 accounts in 1984.

This performance supports what our research told us: there is a vast middle market that is being overlooked by traditional financial service institutions.

Which brings me to the final subject, the impact of new approaches to the delivery of financial service products. This is the area that best illustrates the changing demographics in the U.S. population and the industry's response to them: A growing number of two wage-earner families; reduced periods of time for conducting basic financial service transactions; at one end of the spectrum, a mini baby boom; at the other end of the spectrum, a growing elderly population. The response by providers of financial services to each of these segments of the population is to search for new ways to provide products and services in a faster, more convenient method.

Technology has played a large role in this area. Some providers have handled this approach better than others. For example, certain banks have developed special ATM's which can be used easily by the elderly or the handicapped.

THE DISCOVER CARD

With that as a background, Sears has attempted a new approach to the delivery of automated financial services. Initially, Sears will do this through a product that customers will soon know well—a credit card called the Discover card. However, this will not be just another garden variety credit card. Instead, Sears will begin to build relationships with households through the credit card with which consumers are comfortable and then offer from that relationship special opportunities to save and to invest.

As one example of the financial services available now with the card, Discover card members can take advantage of a family savings account that permits family members to establish their own individual savings account in Sears consumer bank, the Greenwood Trust Co., but, for interest rate purposes, the funds are pooled to achieve the higher rates we offer on high individual accounts. This account, since its introduction earlier this year, has been very well received.

As the card matures, more financial services will be offered, accessible by the Discover card. Thus, we hope to achieve a convenient vehicle by which our customers can truly carry around a bank in their billfold.

Mr. Chairman, these are just some of the new methods by which financial services are provided to the ultimate consumer. These innovations, if allowed to freely develop, indeed, if they are allowed to continue, will be beneficial to consumers.

Sears believes, therefore, that this subcommittee should move to address the difficult issues involved in financial service legislation. This should be legislation which has the effect of enhancing the ability of all institutions, within the boundaries of safety and soundness concerns, to provide each of the products their customers demand. Only then will the industry be truly responsive to consumers' needs.

Thank you, Mr. Chairman, for the opportunity to present this testimony and later on I will try to respond to any questions you or your subcommittee members may have.

[The complete prepared statement follows:]

TESTIMONY OF
MR. ROBERT C. WOOD, II
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
CONSUMER BANKING DIVISION
DEAN WITTER FINANCIAL SERVICES GROUP

MR. CHAIRMAN AND MEMBERS OF THIS DISTINGUISHED SUBCOMMITTEE:

IT IS WITH GREAT PLEASURE THAT I APPEAR HERE TODAY TO DISCUSS WHAT BENEFITS THE FUTURE HOLDS FOR CONSUMERS OF FINANCIAL SERVICES.

TO ENSURE THAT THE GROWTH AND INNOVATION OF THE INDUSTRY CAN PROCEED ALONG LOGICAL AND, INDEED, HEALTHY LINES, MR. CHAIRMAN, SEARS BELIEVES THIS COMMITTEE SHOULD PROCEED WITH LEGISLATION. THAT LEGISLATION SHOULD ALLOW INSTITUTIONS THE GREATEST AMOUNT OF FLEXIBILITY TO MEET THE NEEDS OF THEIR CUSTOMERS WHILE, AT THE SAME TIME, GIVING REGULATORS THE TOOLS NECESSARY TO DEAL WITH A DYNAMIC FINANCIAL SERVICE ENVIRONMENT.

HAVING SAID THAT, LET ME TURN TO THE ISSUE BEFORE THIS SUBCOMMITTEE WHICH IS HOW CONSUMERS BENEFIT FROM A COMPETITIVE FINANCIAL SERVICE MARKETPLACE. IN DOING SO, I WOULD LIKE TO COVER THREE AREAS: FIRST, THE STARTING POINT OF THE SUBCOMMITTEE'S DELIBERATIONS SHOULD BE THE NEEDS OF CONSUMERS IN THE FINANCIAL SERVICE INDUSTRY; SECOND, THE CONCEPT OF "ONE STOP SHOPPING" AS ONE APPROACH TO DELIVERING FINANCIAL SERVICE PRODUCTS TO CONSUMERS; AND, FINALLY, NEW APPROACHES TO THE DELIVERY OF FINANCIAL SERVICES.

MR. CHAIRMAN, AS THE ISSUE OF THESE HEARINGS INDICATES, WE BELIEVE THAT THE STARTING POINT FOR CONSIDERATION IS ALWAYS THE CONSUMER. WE ALSO UNDERSTAND THAT CONSUMERS ARE NOT KNOCKING ON DOORS ON CAPITOL HILL TO BE HEARD ON THE ISSUE OF THE FUTURE OF THE FINANCIAL SERVICE INDUSTRY. CONSUMERS GENERALLY BUY SOLUTIONS, NOT THINGS. THAT'S THE WISDOM IN THE OLD MARKETING MAXIM EXPLAINING WHY PEOPLE BUY QUARTER-INCH DRILL BITS. THEY REALLY DON'T WANT QUARTER-INCH DRILL BITS. WHAT THEY WANT IS QUARTER-INCH HOLES.

THAT IS AS TRUE IN FINANCIAL SERVICES AS IT IS IN THE HARDWARE BUSINESS. THE CONSUMER WANTS SOLUTIONS -- NOT

PARTICULAR INSTITUTIONS. CONSUMERS DO NOT WANT STOCK BROKERS, BANKS, OR INSURANCE COMPANIES. THEY WANT EFFECTIVE DELIVERY SYSTEMS FOR FINANCIAL SERVICES. THEY WANT THEIR FINANCIAL AFFAIRS HANDLED EFFICIENTLY AND PROFESSIONALLY WITH FULL ASSURANCE OF SECURITY. CONSUMERS WANT ALL OF THOSE QUALITIES OFFERED AT A CONVENIENT, ACCESSIBLE PLACE. ONCE THOSE OF US IN THE FINANCIAL SERVICES BUSINESS UNDERSTAND THOSE NEEDS AND MEET THEM, THE CONSUMER BENEFITS. IN THAT PROCESS, BUSINESSES AND ULTIMATELY THE ECONOMY BENEFIT AS WELL.

OUR MARKET RESEARCH REGARDING CONSUMER PREFERENCES CONFIRMS THESE STATEMENTS. SEVERAL SURVEYS OF CONSUMER RESPONSES THAT SEARS HAS UNDERTAKEN OVER THE YEARS REVEALED THESE CONSUMER PREFERENCES.

- 71 PERCENT SAID THAT A CENTRAL LOCATION TO HANDLE ALL CONSUMER TRANSACTION NEEDS WAS A GOOD IDEA; AND
- RESPONSES INCLUDED COMMENTS ABOUT LIKING THE ONE STOP SHOPPING IDEA AS WELL AS TIME AND GASOLINE SAVINGS.

THE SECOND POINT THAT I WOULD LIKE TO DISCUSS -- THE CONCEPT OF ONE STOP SHOPPING -- PROCEEDS FROM THOSE STUDIES AND MARKET RESEARCH.

THERE IS A DESIRE ON THE PART OF CONSUMERS TO CONDUCT THEIR FINANCIAL TRANSACTIONS WITH THE CONVENIENCE AFFORDED BY ONE STOP SHOPPING. THAT IS NOT TO SAY THAT ALL CUSTOMERS PREFER ONE STOP SHOPPING. INSTEAD, SEARS BELIEVES THERE IS A LARGE SEGMENT OF THE POPULATION WHICH HAS NOT ESTABLISHED RELATIONSHIPS WITH TRADITIONAL PROVIDERS OF FINANCIAL SERVICES IN THEIR TRADITIONAL PLACES OF BUSINESS WHO WOULD PREFER THE CONVENIENCE OF ONE STOP SHOPPING.

BY WAY OF ILLUSTRATION, ATTACHED TO MY TESTIMONY ARE THREE CHARTS WHICH SINGLE OUT THE CONDITIONS IN THE SECURITIES BROKERAGE INDUSTRY AS OF 1980. THESE CHARTS DEMONSTRATE THE RELATIONSHIP BETWEEN ALL U.S. HOUSEHOLDS, BROKERAGE CUSTOMERS AND SEARS CUSTOMERS BY LEVEL OF HOUSEHOLD INCOME. THEY ARE ANOTHER WAY OF PORTRAYING THE COMPOSITION OF THE EXISTING AND POTENTIAL MARKET FOR SECURITIES-BASED FINANCIAL SERVICE PRODUCTS AT THE TIME WHEN SEARS WAS CONSIDERING ITS ROLE IN PROVIDING SECURITIES TRANSACTIONS TO CONSUMERS.

BRIEFLY, THE FIRST CHART COMPARES THE INCOME DISTRIBUTION OF ALL BROKERAGE ACCOUNT HOLDERS WITH THE U.S. POPULATION. IT IS SIGNIFICANT TO NOTE THAT WHILE THE PROPORTION OF HOUSEHOLDS HAVING ACCOUNTS RISES DRAMATICALLY ABOVE $50,000 INCOME, THE BULK OF THE ACCOUNTS WERE IN THE $20,000 TO $30,000 SEGMENT. THAT IS THE SEGMENT WHICH SEARS ALREADY SERVES QUITE WELL IN THE MERCHANDISING AREA.

THE SECOND CHART SHOWS THE VAST NUMBERS OF SEARS CUSTOMERS WHO FALL INTO THESE INCOME CLASSES. WITH THE EXCEPTION OF THE TWO HIGHEST INCOME LEVELS SHOWN, THERE WERE MANY MORE POTENTIAL CUSTOMERS FOR SEARS THAN THERE WERE EXISTING BROKERAGE CUSTOMERS IN THE VARIOUS INCOME LEVELS.

FINALLY, THE THIRD CHART DEMONSTRATES THAT CURRENT BROKERAGE CUSTOMERS ARE ALSO CUSTOMERS OF SEARS MERCHANDISING OPERATIONS.

THIS INFORMATION, AS WELL AS OTHER CONSIDERATIONS, FORMED THE BASIS FOR OUR ENTRY INTO THE SECURITIES INDUSTRY IN ORDER TO SERVE THIS LARGE SEGMENT OF THE SECURITIES MARKET. WE SUBSEQUENTLY PUT TOGETHER OUR VERSION OF ONE STOP SHOPPING -- OFFICES OF DEAN WITTER, COLDWELL BANKER, ALLSTATE AND, IN CALIFORNIA, SEARS SAVINGS BANK IN ONE LOCATION IN

EACH OF 313 SEARS STORES. OUR EXPERIENCE WITH THOSE SEARS FINANCIAL CENTERS -- CREATED IN RESPONSE TO A NEED AND A MARKET -- HAS BEEN GOOD. OUR EXPERIENCES WITH COLDWELL BANKER, ALLSTATE AND SEARS SAVINGS BANK HAVE ALSO BEEN VERY POSITIVE.

BEARING IN MIND THE CHARTS REVIEWED EARLIER IN MY TESTIMONY, LET ME REVIEW DEAN WITTER'S EXPERIENCE IN THE FINANCIAL CENTERS AS THE SECURITIES BROKERAGE PART OF THE OPERATION:

- 35 - 40 PERCENT OF DEAN WITTER'S NEW ACCOUNTS ARE OPENED THROUGH THE CENTERS.
- 80 PERCENT OF THESE ACCOUNTS ARE EITHER FIRST TIME BROKERAGE ACCOUNTS OR REACTIVATED ACCOUNTS REPRESENTING NEW CAPITAL TO THE INDUSTRY.

THESE STATISTICS OVERALL SHOW THAT SEARS TARGETING OF A LARGE UNTAPPED SEGMENT OF THE SECURITIES MARKET, COMBINED WITH THE CONVENIENCE AND ACCESSIBILITY OF THE SEARS FINANCIAL CENTERS WAS VERY EFFECTIVE.

* Over two thirds of these customers had stocks in their portfolios.
* Eight of ten visitors to Sears Financial Centers said that Sears has done an excellent or good job of bringing together financial services in one place.
* Finally, in 1985 alone, Dean Witter opened over 200,000 accounts through this system -- up from 154,000 accounts in 1984.

This performance supports what our research told us: There is a vast middle market that is being overlooked by traditional financial service institutions.

Which brings me to the final subject, the impact of new approaches to the delivery of financial service products. This is the area that best illustrates the changing demographics in the U.S. population and the industry's response to them: A growing number of two wage earner families; reduced periods of time for conducting basic financial service transactions; at one end of the spectrum -- a mini baby boom, at the other end of the spectrum -- a growing elderly population. The response by providers of financial services to each of these segments of the population is to search for new ways to provide products and services in a faster, more convenient way.

Technology has played a large role in this area. Some providers have handled this approach better than others. For example, certain banks have developed special ATMs which can be used easily by the elderly or handicapped.

With that as a background, Sears has attempted a new approach to the delivery of automated financial services. Initially, Sears will do this through a product that customers know well -- a credit card called the Discover Card. However, this will not be just another garden variety credit card. Instead, Sears will begin to build relationships with households through the credit card with which consumers are comportable and then offer from that relationship special opportunities to save and to invest.

As one example of the financial services available now with the card, Discover Card members can take advantage of a "Family Savings Account" that permits family members to establish their own individual savings accounts in Sears Consumer Bank -- Greenwood Trust -- but, for interest rate purposes, the funds are "pooled" to achieve higher rates of return for each of the individual accounts. This account, since its introduction earlier this year, has been very successful.

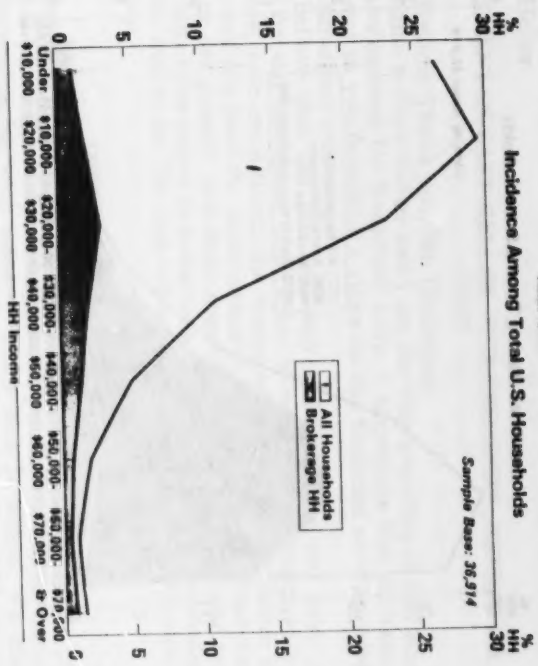
AS THE CARD MATURES, MORE FINANCIAL SERVICES WILL BE OFFERED, ACCESSIBLE BY THE CARD. THUS, WE HOPE TO ACHIEVE A CONVENIENT VEHICLE BY WHICH OUR CUSTOMERS CAN TRULY CARRY AROUND A BANK IN THEIR BILLFOLD.

MR. CHAIRMAN, THESE ARE JUST SOME OF THE NEW METHODS BY WHICH FINANCIAL SERVICES ARE PROVIDED TO THE ULTIMATE CONSUMER. THESE INNOVATIONS, IF ALLOWED TO FREELY DEVELOP -- INDEED, IF THEY ARE ALLOWED TO CONTINUE -- WILL BE BENEFICIAL TO CONSUMERS.

SEARS BELIEVES, THEREFORE, THAT THIS SUBCOMMITTEE SHOULD MOVE TO ADDRESS THE DIFFICULT ISSUES INVOLVED IN FINANCIAL SERVICE LEGISLATION. THIS SHOULD BE LEGISLATION WHICH HAS THE EFFECT OF ENHANCING THE ABILITY OF ALL INSTITUTIONS, WITHIN THE BOUNDARIES OF SAFETY AND SOUNDNESS CONCERNS, TO PROVIDE EACH OF THE PRODUCTS THEIR CUSTOMERS DEMAND. ONLY THEN WILL THE INDUSTRY BE TRULY RESPONSIVE TO CONSUMERS' NEEDS.

THANK YOU, MR. CHAIRMAN, FOR THE OPPORTUNITY TO PRESENT THIS TESTIMONY. I WILL TRY TO RESPOND TO QUESTIONS THAT THE SUBCOMMITTEE MAY HAVE.

CHART 1



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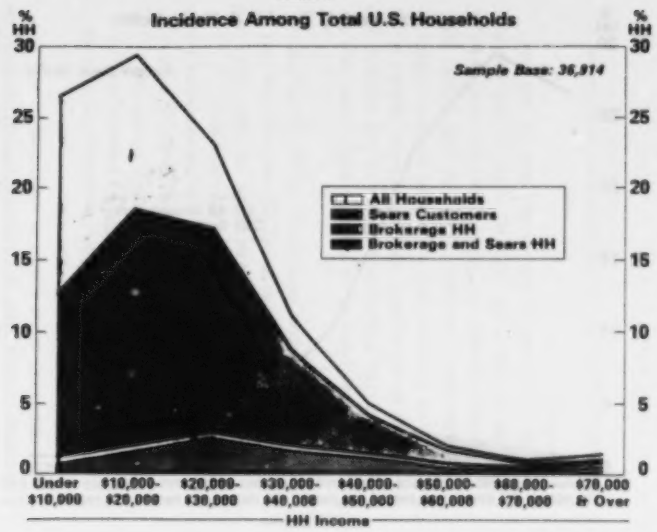

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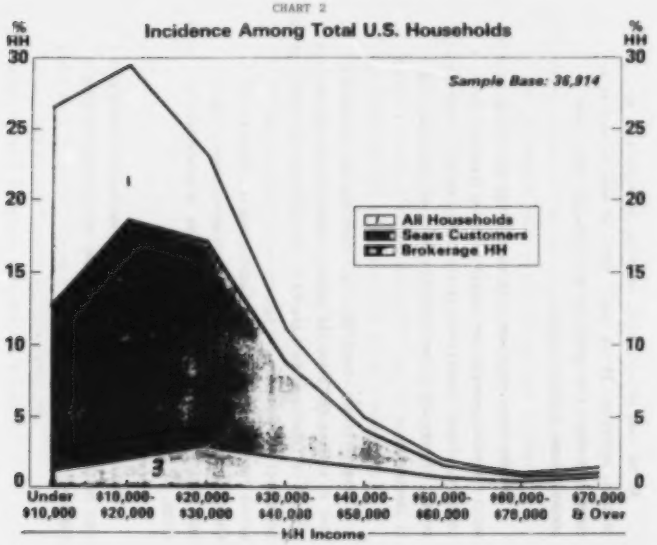

Senator GORTON. Thank you, Mr. Wood.
Mr. Heller.

STATEMENT OF GARY HELLER, VICE PRESIDENT, BENEFICIAL CORP.

Mr. HELLER. Thank you, Mr. Chairman.

My name is Gary Heller and I am the vice president of new business development for Beneficial Corp. I appreciate this invitation to present to you Beneficial's views on the financial services needs of the American consumer.

We believe that the role you play and the focus you have assigned for our discussion here today is of vital importance to our customer, your constituent, the American consumer. His desire for choice and his need for convenience in the financial services marketplace are greater now than ever before. Deregulation and new technology have begun to make these benefits available, particularly to the well to do. The task before us is to make them available to everyone.

CONSUMER FINANCIAL SERVICES

It may help to place my remarks in context if I tell you that Beneficial is one of the Nation's largest independent consumer fiancial services companies, with assets of more than $8 billion. We make mortgage loans, both first and second. We make personal loans and small business loans. We issue insurance policies and credit cards and we do income tax returns.

Now I stress the term-consumer finance. We do virtually no business whatsoever with foreign governments or giant customers. Our 2 million borrowers, cardholders, and customers are mostly typical middle-class Americans. They have household incomes between $20,000 and $50,000 per year, a range which puts them right in the mainstream of our economy.

As head of new business development at Beneficial, I, too, study the same question that you are addressing at these hearings: What does the American consumer want from financial institutions such as ours?

The consumer does not usually answer this question directly. We never had a customer walk into one of our loan offices, for example, and say, "I wish you offered a retirement annuity that I could fund through my IRA contributions." But when we sat down with our customers and discussed their financial objectives and then asked them if they would like such a product, they gave us a loud and clear "yes." And when we began this year to sell those IRA-funded annuities, they backed those "yes" answers with their savings dollars.

In fact, that has been the dominant pattern of Beneficial customers. They have voted overwhelmingly with their checkbooks for greater choice and convenience in the financial services offered to them.

We've spoken a lot about this revolution in financial services and the two driving forces behind it: First, deregulation at both the Federal and State levels has spurred both new entrants to the industry and new products and services for the customer. Second,

technology has provided the execution and delivery systems to make those products and services possible.

But we think there's a third force behind this revolution—the consumer. The economic turbulence of the last 10 to 15 years has stimulated an unprecedented level of economic literacy among average Americans. They are sophisticated and they understand that money, even at low-income levels, must be managed, not just spent or saved. They are involved. They have numerous sources of financial guidance and information. They want to make the key decisions themselves. Their watchword is choice—the same choice they exercise in the rest of their lives.

The changing consumer demographics impose a different necessity. For those of us who grew up in households with two adults and one income, it comes as a shock to realize that they now comprise only 19 percent of all American households. Households in which both adults work, or in which there is only one adult to do everything, want above all else convenience.

They insist on making their own decisions, but they have limited time to implement them. A full-service provider is enormously appealing to today's consumer. A recent study by Synergistics showed that of households earning less than $35,000 a year—and that's more than half the country—26 percent already have a single-provider of financial services and 61 percent would consider having one, an improvement over what they've got now, a total of 87 percent who look to having a single provider of financial services.

CHOICE AND CONVENIENCE

These are the two consumer characteristics that our ongoing financial services revolution is starting to bring to the American population. I say starting to advisedly because financial institutions began their innovations with their most profitable customers: Large corporations and affluent individuals. Only now are we seeing these benefits reach the base of the economic pyramid.

The question before us is: Will the institutions that serve the average American household be free to offer a full range of products and services to the public or will they be limited to specific activities? Except for regulations that bind them, there is really little difference today between banks and finance companies, brokerage houses and insurance companies.

We believe strongly that all of them, and all other legitimate financial institutions, should be free to compete with each other throughout the full range of financial services so that the consumer himself decides who will supply him with what services and at what price.

In conclusion, the opening of the financial services marketplace has begun to provide the average consumer with greater choice, greater convenience and, ultimately, greater value for his time and his money. We urge that any action taken by this committee continue in the direction of accessible marketplace, open competition, and maximum consumer benefit.

Thank you.

[The complete prepared statement follows:]

STATEMENT OF

GARY R. HELLER

BENEFICIAL CORPORATION

Mr. Chairman, members of the committee, my name is Gary Heller. I am a vice president of Beneficial Corporation, in charge of new business development. I appreciate this opportunity to present to you Beneficial's views on the financial service needs of the American consumer.

To place Beneficial in context, we are the nation's largest independent consumer finance company. We have more than two million customers. We serve them from a network of more than 900 retail offices and consumer service locations around the country. We have over $8 billion in assets and a net worth exceeding $1 billion.

We provide our customers with a broad range of consumer financial services. Our name has been synonymous with personal loans for generations, and this is still one of our major businesses. But we are also the largest originator of second mortgages in the country, and we are now building a major presence in first mortgages as well. We are one of the largest issuers of Visa and MasterCards. We are active in financing small businesses. We own a savings bank and a commercial bank. We offer a variety of insurance products. And only H & R Block prepares more income tax returns than we do.

As this should indicate, we are a consumer finance business:

we do virtually no business with foreign governments, nor with giant corporations. Our two million customers are, for the most part, typical middle-class Americans. A high percentage of them have household incomes between $20,000 and $50,000 per year, which puts them right in the mainstream of the economy. We are vitally interested in their needs and interests and well-being; our prosperity is a direct reflection of their own.

As head of new business development for Beneficial, I am directly concerned -- though obviously in a somewhat different way -- with the same questions you are addressing in these hearings: What are the financial services needs of the American consumer? And how best can a financial institution like Beneficial meet those needs? We have studied these questions in considerable depth. Several recurrent themes have emerged, and I would like to summarize them for you.

Theme I — There has been a basic and permanent change in the dynamics of delivering financial services to the consumer. This shift has implications in the economics and marketing of financial services products.

Continued...

In the past, the traditional financial services company initiated and executed all of the functions necessary to deliver financial services to the consumer, whether this was the "manufacturing," "wholesaling," or "retailing" of assets and/or liability services. All the steps in the distribution chain -- product development, risk management, funding, marketing, promotion, sales and service -- were originated and controlled by the organization providing the product to the consumer. In some cases this was an insurance product; it could just as easily have been an asset or liability product, a trust, or investment advisory and brokerage services.

Deregulation and the advances of technology have presented an economic challenge to financial services companies. Deregulation provided them with the opportunity to enter new fields; but it also meant their own fields could equally be entered by new competitors. Technology, meanwhile, gave all participants not just the ability to do a great deal more, but to do it better, faster and less expensively.

The response of many major financial services companies has been to reduce their vertical service integration and broaden the scope of the functions at which they are best. For some institutions like consumer finance companies and local banks, that has meant a

Continued...

greater focus on direct delivery and distribution of financial services to consumers.

Focusing on a functional specialty in this way has given financial services companies broader service capabilities in meeting consumers' varied needs. They can now offer a more comprehensive array of products, supporting quality services backed by profits and solid resources.

Moving from a vertically structured organization to an increasingly horizontal structure has benefitted the consumer in two ways:

(1) All steps in the distribution chain are supported by state-of-the-art technology and institutional expertise, though the same institution might not be represented in each step.

(2) Delivery and distribution to the consumer offers a broader variety of options, at a lower price, in response to the consumers' needs.

These advantages to the consumers have not gone unnoticed by members of the competitive community: Commercial banks, savings

Continued...

institutions, insurance companies, consumer finance companies and brokerage houses. These once-quiet institutions have become aggressive marketers, and consumer benefit has become the cornerstone of their marketing campaigns. Through newspaper articles, seminars, periodicals, television, and advertising, American consumers are constantly reminded that they are better off because of the revolution in the types of financial services that now can be offered to them.

American consumers have acknowledged this revolution, and they have responded to it. From the market research that has been conducted, and -- more directly -- from the actual behavior of the consumer over the last several years, two overriding consumer imperatives have become inescapable:

First, choice is now a paramount goal of the American consumer. Time and again, in every way possible, the public has told us it wants more, not fewer, options. They want any institution with which they deal to present them with the fullest possible menu of alternatives. And they want the institution to "empower" them to make their own choices, from the variety of options offered to them.

A corollary to this principle is that consumers want to

Continued...

make decisions supported by "expert information." They want the financial services company to provide some of this information; they also want to gather information independently, from the media, from professional advisers, from the opinions of friends and relatives, and from other sources.

Second, once a consumer has made his decision, he wants quick, accurate, inexpensive implementation with minimal effort on his own part. The demographics of our society have changed. The same consumer who will spend his evenings poring over prospectuses and financial publications has no time during conventional working hours to implement his decisions.

The stereotypical American family has two adults, one of whom works to generate income, the other of whom manages the household. Today, that classic family accounts for only 19 percent of American households. The vast majority of households contain either one adult who must do everything for the household, or two adults, both of whom work, and who therefore have limited time for the transaction of family financial business.

This is where integrated financial services comes in. It is not so much in the decision-making process, but in the execution. It is perhaps best thought of as one-stop implementation, rather than one-stop shopping.

Continued...

Personal financial planners repeatedly hear that the client expects the planner to manage and execute a total program. The same is true of loan officers, bank managers, stockbrokers, and anyone else whose profession includes giving financial advice to consumers. If the advice is accepted, the next question is always, "can you do it for me?" The advisor would not necessarily perform all of the services in-house, but act as the intermediary or managing director, coordinating the delivery of many financial services.

Beneficial's continuing goal is to leave the financial decision-making in the hands of the consumer, while providing a well-rounded portfolio of services to support his ultimate decisions. We are especially interested in providing implementation and delivery support that matches the customers' needs for convenience, reliability, timeliness and accuracy.

In many cases, these needs suggest a combination of services and products bundled in a single package.

These are the needs of average American consumers, who now have an unprecedented level of economic literacy. They understand that money, even at low income levels, must be managed, not simply spent or saved. They insist on making their own decisions, but they have limited time to implement them. This is the reason

Continued...

"one-stop" financial planning is so appealing to today's customers. I note a recent Synergistics study showing that 87% of households earning less than $35,000 (and that constitutes more than half the country), either have a single provider of financial services or else would consider a single provider an improvement over what they presently have.

Theme II — More is not necessarily better. Despite the imperatives of consumer choice and convenience, all products are not appropriate to all consumers or to all providers.

The economic turbulence of the late 1970s and early 1980s produced better informed consumers whose active interest in financial affairs has grown over the years. Their increased sophistication and the expansion of financial services has resulted in a significant growth in spending on these services and an increased demand for these products.

This increased demand has, in part, led banks and other finance companies to broaden the scope of products offered through their distribution system. But it is clearly not appropriate to

Continued...

force every possible product through every distribution system. Not only are all products not appropriate to the needs of all consumer segments, but, no matter how appropriate for the consumer, some products do not lend themselves to bundling with other financial services.

Our research has shown that each segment demands some degree of product bundling, that is, the combination of different products and services into menus and packages from which the consumer can choose. Over time, consumers are coming to prefer intermediary, advisory and execution services to help them deal with the avalanche of new and different products. For simplicity and convenience they will want these services consolidated at a single company, a further indication of a preference for one-stop shopping.

We see different demands to consolidate services from different segments: Younger consumers need loan, transaction, and life insurance products. Older Americans have less need for life insurance coverage and they are not frequent borrowers; they demand health insurance, investment and insurance products.

But just as all consumers are different, all providers are different. Every financial institution has services at which it excels, and others which it cannot provide well, or profitably.

Continued...

So each institution will create its own bundle of products and services, corresponding not just to its perception of the market, but also to its particular competence.

Financial service companies will need both the flexibility to offer a range of services and a sensitivity to the changing needs of consumers. With those factors in mind, product bundling -- one-stop shopping -- will produce more responsive service to the customers, with the improved economies of distribution passed along in improved prices.

Theme III Financial services must be built on trust and confidence. Despite the impact of new technology, traditional relationships remain a powerful factor in the marketplace.

At Beneficial, we are fond of saying that the best research on the American consumer is done daily by the men and women in our field offices. They hear directly what service means to their clients. It appears that the "relationship concept" in financial services is a human phenomenon, not one of product.

Continued...

The human contact behind the product leads consumers to prefer "one-stop shopping" over single products. Consumers perceive an added value in the counsel and assistance of qualified representatives of financial services. They do not expect one individual has all the answers, or even offers all the products. As with financial planners, consumers look to traditional financial managers for direction and consultation. This tendency will increase as products and concepts become more complex.

Only the wealthy used to require this special kind of service. To a great extent, that was more a function of supply than demand. One marvel of today's world is that lower-income people now share in the opportunity to use a broader array of financial services, including revolving credit, investment quality deposit instruments, and specialized insurance and annuity programs, to name just a few.

As these opportunities have reached the largest market, we at Beneficial observed our customers dividing their financial needs into two general categories. One category consisted of what I will call here "pure conveniences," such as credit cards and automatic teller machines. For services such as these, pure utility is the criterion. For now it appears that this kind of service discipline will be limited to products requiring fewer investment decisions

Continued...

and more, short-term, consumption-driven needs: Cash, payments, simple savings and routine financial asset movements (on and off the balance sheet).

But for what I will call "judgment services," the consumer has shown that he wants to know the person who will assume responsibility for executing his wishes and handling his affairs. We see an increasing demand for traditional relationship services combined with responsiveness, understanding and communication.

If there is a subsidiary trend in the offing here, I suggest it will be this: The consumer will increasingly select his provider of pure convenience financial services on the basis of simple cost and convenience. But he will select his judgment-based services from other providers, with his selection based on such other criteria as the track record of the provider and the quality of the personal relationship he is able to establish with those with whom he deals.

Theme IV — There is no "mass market." There is, instead, an enormous diversity of needs, tastes and interests among the consumers of financial services.

Continued...

The economic, social and cultural differences across the country reflect different needs among consumers. Beneficial has served its regional markets through many shifts in demand, high and low periods, adjusting our products and our goals according to the marketplace. Although there is greater homogeneity among consumers than ever before, a diversity in needs and preferences, very often reflecting demographic shifts, are very observable and measurable facts.

To deal with these diverse needs effectively, national financial institutions must have a broad range of product and delivery options if they are to address the consumer market effectively. We, and other institutions like us, must have the ability to respond to the unique needs of our markets on a regional as well as a segmented basis. We must have the capability to deliver a broad spectrum of products so that when demand shifts are anticipated, we are able to meet our markets' needs with new financial strategies in a timely fashion. These responses cannot be makeovers of products or services designed for other markets.

Continued...

Summary

1) Because of the structural and regulatory changes in our industry, some companies will specialize in delivery to the consumer, others in wholesaling and brokering assets and liabilities through institutional channels. Still others will originate and distribute new vehicles created in the first areas.

(An example might be Beneficial's bank experiment in Florida, where we are testing the hypothesis that a diverse offering of products and services is viable. Another example; we are integrating insurance products with credit products in an effort to fulfill both an immediate consumer need, such as a loan, with a longer term need, such as an investment.)

Breadth of service will be necessary for any institution, regardless of its rung on the distribution ladder. As we specialize in our chosen markets, we must have the ability to deliver full services.

2) There is no single answer to serving the consumer today or in the future. The consumer has become sophisticated and his demands are complex and diverse. Accordingly, so are his

Continued...

purchase and consumption preferences. We believe the consumer will continue to demand product packages and "bundles" for some services, and will use other financial services on an individual basis.

3) A broader range of financial services and products has been offered to the public as a result of deregulation and advances in technology. As a result, middle market consumers have expanded their use of financial services and perceive a greater value in "service relationships." These relationships are perceived as sources from which other financial transactions will originate. This trend will increase as more products are introduced.

(For example, Artificial Intelligence Technology, has the potential of serving the needs of the consumer in more aspects of financial opportunities, as well as allowing consumers to change the types of relationships they have with an institution.)

It is an oversimplification to assume that consumers represent a "mass market." The needs and wants of consumers are very sensitive to economic, social and cultural characteristics in a region. We believe that public policy should take these differences into account.

Continued...

This means that financial services institutions should operate in a regulatory environment that defines financial services broadly enough to permit all institutions to use their strengths effectively and to address constructively the needs of the consumers they seek to serve. An institution that cannot tailor a broad range of products and services to the needs of specific segments of the population will neither prosper nor survive.

This ability to compete freely through the full range of financial services is what will make possible better services for disadvantaged and under-served segments of the population. But it is also what will make certain the availability to a full range of financial services -- at low and competitive prices, not just to large corporations and the wealthy, but to the entire citizenry of our nation, rich and poor, rural and urban, old and young.

We urge that any action taken by this committee encourage the accessibility of the financial services marketplaces to all legitimate financial institutions, and to foster free competition between them, and thereby to provide maximum consumer benefit.

E N D

Senator GORTON. Thank you, Mr. Heller.

Both of you, of course, were here to listen to Mr. Kehrer speak about his interpretations of the Federal Reserve Board's consumer survey and to hear the remarks of Senator Proxmire about the surveys which he has included in the record.

INCONSISTENT NATURE OF SURVEYS

You at least, Mr. Wood, referred to your own internal research. Do either or both of you have surveys which are comparable to those we've heard testimony about so far today which are other than simply internal to which you could refer and which you could provide for us, and what comments do you have on the somewhat inconsistent nature of the surveys about which we have heard? I'd be happy to hear from both of you on that subject.

Mr. HELLER. Well, the survey that I referred to was provided to us by Synergistics. It's a syndicated study and, very frankly, I had to get permission from them to cite it for the record. But they, in fact, did a survey that covered the middle market, so to speak, and it's really our traditional customer, the $35,000 and under household.

Their research appeared to substantiate what we heard Mr. Kehrer say earlier.

With regard to the comments by Senator Proxmire, from our own vantage point, we serve a distinctly different marketplace than those individuals who responded to the survey that the Senator referred to.

Senator GORTON. So from your point of view it doesn't matter whether that was true or not?

Mr. HELLER. Well, I wouldn't go that far. But as far as our own market is concerned, we feel that the research that we have done and that we are privy to substantiates the need for consolidation of financial services for that marketplace that we serve.

Senator GORTON. Mr. Wood.

Mr. WOOD. Sears has done research both internally—through our own market research department—as well as bought external research. I cannot state exactly what those surveys are. We will provide, however, your subcommittee with the information we have.

Essentially, though, I think the surveys agree in principle with what Mr. Kehrer indicated here. There certainly is, we have found, among all areas of the population a substantial interest in either one-stop shopping or certainly more convenient access to financial services.

I think maybe you can take the one-stop shopping a little bit too far, but what we have found is that our customers in the Sears financial centers appreciate the ability to come in evenings and on weekends when our stores are open, understanding that more than half of the American households have two wage-earners today, traditional banking hours, if you will, just aren't convenient for a lot of consumers. So we think the convenience that we offer is perhaps the most responsive thing we are doing to the surveys that we've seen.

But we do agree largely with what Mr. Kehrer indicated.

Senator GORTON. Fine. If you could supply us with your survey information, it would be helpful. And if yours is available, Mr. Heller, it would be of some help to us.

[Information requested was not received in time of publication.]

I'm now going to quote a paragraph of Fed Chairman Volcker's testimony recently on this subject and ask each of you to comment on it.

Mr. Volcker said:

> By permitting commercial companies to provide through subsidiaries almost all the same functions as full-service banks, both the principle and practical reality of the present restrictions of the Bank Holding Company Act will be seriously undermined over time. The competitive position of those banks subject to the act will inevitably be damaged, potentially weakening the system as a whole.

Is that a legitimate concern in your view?

TWO-WAY STREET THROUGH DEREGULATION

Mr. HELLER. I have some concerns about that issue and I think that it's probably more a sense than substantive. I feel that as financial institutions are allowed to expand the services and products that they offer—it's sort of a two-way street—through deregulation, it's almost implying that there will be closer scrutiny and closer control of the new activities that these institutions are allowed to provide.

For example, a traditional commercial bank which has always been under the scrutiny of both internal and external auditing policies, if they were to add insurance products they would then be under the scrutiny of individual insurance commissions and a similar situation would occur were they allowed to offer brokerage services.

So I think that what we've seen, in essence, is deregulation allowing a wider range of services but, at the same time, allowing for due diligence, which I feel would not cause any harm to the institutions.

Senator GORTON. What about the other side of that coin, Mr. Heller? I think Chairman Volcker is concerned with the fact that allowing companies like yours into what have been traditional banking functions without this regulation that that will hurt banks in their banking functions and, therefore, weaken the system as a whole.

Mr. HELLER. Well, I think that the most vulnerable part of any banking operation is the lending of funds. I think that many of the new services that we're talking about adding, or hopefully adding, are more on the investment side. I think that these are less risk oriented certainly than loans. I'd like to think that over our 71 years of history we've sort of got that down to a formula—how to loan money and still control the corporation. So I'm not sure that I would agree with that statement in its entirety.

Senator GORTON. Mr. Wood.

Mr. WOOD. Certainly some of Mr. Volcker's comments about the changing conditions and the impact on the Bank Holding Company Act are true. We obviously question whether the Bank Holding Company Act is right for today.

In terms of the safety and soundness of the banking system, we are very anxious to see that maintained. We depend on hundreds

of banks across the country everyday to support our operations and have no interest in seeing the role of major banks impaired in anyway. We don't think our activities in the banking industry will.

As I think you know, we do support the right of traditional banks to offer expanded services such as securities and insurance. At the same time, we believe that the consumer and the economy are best served if other nonfinancial institutions, should they choose, be able to offer banking services as well.

Anything that offers the consumer more choice in a free economy is ultimately good for the economy, in our opinion.

Sears has owned the Sears Savings Bank since 1958. We have been lending to consumers since 1911. So in a sense we have been in the banking business for a long time and I think those who have dealt with us would find that we have done that very responsibly.

Senator GORTON. But you don't feel it either unfair or dangerous that you get into major forms of banking and become a part of the payment system but not be regulated as a bank?

Mr. WOOD. Well, we support regulation in the form of the safety of deposits and the payment system and things such as that. When we talk about deregulation we are not extending that to the safety of deposits. We do believe that we would not in any way impair the safety of the payment system or the banking business at all. No, we see no reason to come to that conclusion.

Senator GORTON. If Congress goes along with your request and the marketplace evolves as you would like to see it evolve, what kinds of products or services that consumers desire are most likely to take place? Can you predict both the type and the quantity of such services that will result from one-stop financial services or is that something that will only evolve when the ability to use your imagination is there?

Mr. HELLER. Well, we like to think that we're a market-driven company. Every company likes to think of themselves as market-driven responding to the needs of the marketplace and the consumer. We feel that—and I think most financial institutions would agree—that the whole area of financial planning, which is difficult to define because it means different things to different people, is certainly an area of opportunity for most financial institutions.

What this entails is probably expansion of investment products from traditional FDIC-guaranteed products to mutual funds, money funds, unit investment trusts, and other investment products along those lines.

We feel that in a full financial plan that many aspects of an individual's life, such as tax preparation, estate planning, planning for a child's education, and retirement planning, that all need to be served and spoken to. And we have found from our own customers that they would just as soon sit down with us because they feel comfortable with our employees and have us help map out a plan for them. So I think what we're looking at doing there would be expanding the number of services and the number of products that would be made available to our consumer so he could fulfill those needs.

Mr. WOOD. I would agree with that statement entirely. I suppose the focus of where we would be is our professional account executive. We have 7,000 of them now. They are Dean Witter account

executives. But in today's world they are providing much more than the traditional stock and bond buying and selling function. In fact, a very small percentage of what our customers are buying today are individual stocks and bonds but rather packaged products, whether they be mutual funds or other investments like certificates of deposit, IRA's. We found a great comfort on the part of the customers visiting our Sears financial centers to talk with a professional account executive about something broader than just what the investment industry, as we've known it in the past, has offered.

In terms of what we might offer, as you suggest, that's hard to put your finger on right now. We have to get into it first. Whatever we do, I think banks are going to be offering them as well and we expect a very competitive marketplace. But I am not suggesting that we could offer things that other institutions could not. I think we would develop investments which might not otherwise be offered and in so doing I think that will benefit the consumers. We would expect other people to follow us if the product is right and create what is, in essence, a very competitive marketplace. That, of course, benefits consumers.

FINANCIAL SUPERMARKET

Senator GORTON. This Senator has been a member of this committee now for almost 4 years and it has been repeatedly and forcefully argued to him by those who believe that banks should not be allowed to expand into new products and services that their leverage, because of their ability to grant credit, will inevitably be used to force customers to purchase products and services that either they wouldn't want or, more likely, that they could obtain less expensively elsewhere.

It's pretty clear that the same arguments can be applied to the so-called financial supermarket. Is this a nonthreat, in your view, or are there potential abuses which should be prevented and, if so, how?

Mr. HELLER. Anything that I could comment on would be sheer speculation. I really don't have any information to substantiate that one way or the other.

Mr. WOOD. For my part, I do not believe that is a threat, but we also support affiliate transaction restrictions, many of which exist today. In fact, the legislation in the House which we are supporting has within it some regulatory requirements which are more stringent than the ones which exist today.

We are in favor of antitying provisions which would prevent that type of abuse. I don't think it would happen, but we are in favor of regulations to make sure that it does not.

Senator GORTON. Do you two agree with Mr. Kehrer that customers are relatively indifferent to what financial institutions charge; that is to say, for credit cards, returned checks, checking accounts and the like; and are much more interested in services?

Mr. HELLER. We've found that the real watchword is convenience. Individuals want products and services delivered conveniently, efficiently, and quickly. I think that's really the major issue.

I think that the research that Mr. Kehrer presented would be substantiated by our own customers response.

Mr. WOOD. That is the same for us. I wouldn't say they are insensitive, but the issue of convenience, as long as it's affordable, seems to be paramount to considerations of a specific interest charge or a check fee.

Senator GORTON. What about check hold policies?

Mr. HELLER. Again, I can't really comment on that. I can provide you with some information regarding check holding policies, but I don't have that information available right now.

Mr. WOOD. We agree that consumers should have access to their deposits as quickly as possible and are supporting more stringent requirements in that regard.

Senator GORTON. Would you be likely to deal with any of these issues differently at present than traditional banks do?

Mr. WOOD. That I couldn't comment on. I'm not sure how they would deal with them. We believe that the consumer must be protected and if we believed there was any threat to the safety of the consumer deposits or to the soundness of the banking system we wouldn't be doing what we are.

Mr. HELLER. I think also that if that were to be the situation I think the consumer would respond very loud very quickly.

Mr. WOOD. I agree with that.

Senator GORTON. OK. Thank you both very much. We appreciate your help and your testimony.

We now have a second panel with Mr. Anderson and Mr. Kinst. Mr. Anderson, we will ask you to start.

STATEMENT OF LYNN L. ANDERSON, PRESIDENT AND CHIEF EXECUTIVE OFFICER, FIRST NATIONAL BANK, LAWRENCE, KS

Mr. ANDERSON. Thank you.

Mr. Chairman and members of the committee, my name is Lynn Anderson. I am president and chief executive officer of the First National Bank of Lawrence, KS. I very much appreciate this opportunity to share with you some of my perspectives on the market for financial services and on what I see as the need to redefine the role of commercial banks within that market.

I might tell you a little bit about my community so you'll have some perspective of where I'm coming from. Lawrence, KS, is located just west of Kansas City. We have a population of around 60,000 and that 60,000 includes approximately 25,000 students who are enrolled at the University of Kansas which is located in Lawrence. We have four local banks. Our bank, at $120 million approximately in assets, is the largest bank. We also have the tallest building in downtown Lawrence. It's six stories. So we are a dominant player.

We have four savings and loans. We have seven credit unions and eight finance companies and I believe Mr. Heller's firm is one of those competitors in the finance company business. Additionally, banks like Citibank and Norwest Bank compete in our market area.

But the competition isn't limited solely to those that would be traditional players such as that. We have, for example, on the fourth floor of our tall building a Dean Witter office. Mr. Wood's

firm has an office in our building staffed very ably by a former bank president locally and some other local sales personnel. It's a subsidiary of Sears, as Mr. Wood said, and they are a financial competitor of ours.

Additionally, Investors Diversified Services [IDS], which is a subsidiary of American Express, is also located in our bank building.

What we're finding is that these firms can and do offer a combination of financial products and services that are tailored to the needs of our customers while our bank is tied by regulatory restraints from issuing or competing in that marketplace with similar financial packages.

DEREGULATION IS INACCURATE

The testimony this morning has indicated that there are a number of reasons for the environment change in banking and in the financial services industry and that it's changed dramatically, and I think that's correct. It has changed dramatically. The word deregulation has been used. From our perspective, deregulation is inaccurate. It has been decontrol of interest deposit rates and that has been the extent of deregulation.

We think that the dramatic changes have been brought about by technological advances in the first instance, which have resulted in the creation of new services and affected which institutions can most efficiently produce and deliver the new financial products.

As an example of that, in the computer capacity area which has been developed tremendously, that increased capacity has promoted eventually the use of money market funds by lowering the transaction costs of handling large volumes of small investments.

Another example of the development which has affected our marketplace and our financial services is the development of the ATM networks and the computerized mortgage networks which allow homebuyers to shop nationwide for the best type of mortgage for them.

We think also that there have been significant shifts in the demographics of our community and the demographics of the country. The huge baby boom generation as it reached its thirties created a tremendous demand for housing finance in our market and as they near 40 their demands for other types of products related to future retirement needs or college education of children and so forth are also increasing and this has brought about an increase in the types of new financial products that they are expecting to be provided, either by us or by someone else.

Economic volatility has also affected a change in our banking business. Inflation and volatile interest rates during the past several years has dramatically changed the demand of our customers. Bank depositors, even those who went through the Great Depression who had all kinds of concerns about financial risks saw the value of their fixed-rate deposit investments eroded by inflation and, frankly, they are no longer content to put their money in an insured savings account and forget it. They have become increasingly sophisticated in their choices of financial instruments and they see both the need to diversify their savings for risks and for return.

I personally believe that this is a very positive and a healthy development because consumers should take an active role in the management of their savings and investments. We have recognized that point in our bank and we are currently involved in developing a financial planning program, which we think will help not only our trust customers but our other bank customers as well.

The key need that we find for consumers is advice, advice on how each individual can best use the financial services system to his best advantage.

GROWING NUMBER OF PROVIDER SERVICES

There is a growing number of services, a growing number of providers in the financial services business, and we think customers want and ask for advice on how to use those services.

Now as you can probably guess, what I am basically is a small businessman and I'm managing a small bank. We have a good staff. We have good rapport with our customers and we think that that relationship, plus our knowledge of the local market and our expertise in financial management makes us uniquely qualified to offer this type of financial planning service. This service would be helpful to those who have wealth and who need to protect it. But equally important, it would be helpful to those who are just starting out and need to develop a plan to protect their families and begin providing for retirement, or to develop a savings program of investments for their future needs that were mentioned, like college education.

The frustrating part of this program is that while we can provide some of the services for financial planning and we can provide the financial planning, we can't provide most of the services that would be included in such a plan.

For example, in a financial plan for a young family, it would undoubtedly include the need for life insurance or annuity products, or casualty insurance, all of which are products banks can't sell. Insurance products are very important, we feel, for the risk management for both those that have wealth and those who need to accumulate wealth because they can be used to manage risks and they can be used to accumulate savings.

In many cases we feel it would be far more convenient and perhaps much less expensive for our customers to be able to purchase insurance products directly through the bank. It certainly would be advantageous to at least allow them that competitive option.

There is another similarly important element in a consumer financial plan and that is mutual funds, which again banks cannot sponsor and distribute. Of course, we can offer a collective or pooled investment fund to our trust accounts which we have for years, but we have many other bank customers who would also like to have their money or that vehicle available to invest their funds in a similarly efficient way but who do not have currently a trust relationship nor need one. Basically, we have no way to supply a service that customer's needs.

On the other hand, the Dean Witter office located in our building can offer a full range of securities brokerage services with mutual funds. Potentially, they can offer a full line of insurance products

through the Sears financial network and Allstate insurance. They can offer real estate brokerage and equity participations through Coldwell Banker, and insured deposits through Sears Savings Bank, and a lot of other banklike products.

And while I've got to admit this is not a commercial for Sears or Dean Witter, they do a heck of a good job at that. They are tough competitors.

I have no doubt that many of my existing customers find those services very attractive and I can see no reason why they shouldn't be able to purchase them. I have no doubt as well that many other customers in the future will find them similarly attractive.

The point is, Mr. Chairman, it is very frustrating to develop a financial plan and include in it a number of services which are integral parts of any type of plan, and then have to send our customers someplace else to get those services and those products.

In our business, once you lose a customer, it's very difficult to get them back, particularly if they're handled with quality care and quality convenience.

Let me mention one other example of our ability to meet the customer's needs in this type of market and that relates to the IRA business. This year our bank aggressively promoted IRA deposits. We put in an interest rate that was above the market. We advertised aggressively. We solicited aggressively. And yet we had a zero net gain for 1985 IRA contributions and I have no doubt that without the active marketing program and relatively high interest rates we simply would have lost ground.

Our customers, like many others across the country, seemed this year to prefer to invest in mutual funds or other type securities and basically those products that we could not participate in.

To help fill these gaps, we've recognized that we need to do something, so we now offer a mutual fund share program through Federated Securities Corp. which is a subsidiary of Aetna Life & Casualty Co. That's available to our customers. And we've also considered an arrangement with an insurance company to put a sales desk or a kiosk in our lobby to also offer annuities and insurance-type products.

It's certainly not clear to us that this is the most efficient or the best way to offer those kind of services, but that's what's available to us. We have no other choice at this point.

GREATER DIVERSIFICATION NEEDED FOR BANKS

What we would like is to have a choice of how best to serve our customers. We think that banking is in the business of providing financial services. It is highly competitive. It is service oriented and we are convinced that to be successful our bank must emphasize the quality of treatment of our customers as well as the quality of the products that are sold. We feel that we lose a substantial measure of control over these very important elements by having to contract with outside firms to provide the services that our customers need and which we feel we could provide.

Real estate brokerage is another natural extension of the type of services that we feel should be available to our customers. Buying a house is the single biggest financial decision, the single biggest

purchase, generally that our customers ever have and I'm sure that's true of almost all consumers.

Often our customers will come to us, they will basically talk to us about the kind of housing that's available to them, what they can afford and how they can finance it. We really help make the decision for them. We have presently about 15 percent of our loan portfolio in single family residential mortgages. In addition, because of the nature of the fixed-rate interest rate market, we originate and sell many more mortgages than that in the secondary market. In each case, we are involved in almost every step of the procedure involved in buying a house and yet we get to the point where we have to send the customer away for somebody else to handle the brokerage business.

Let me give you another example of what appear to me to be outmoded legal restrictions that affect a bank and prevent us from helping our customers and our community.

On one occasion we bought an entire issue of a municipal revenue bond issued by our city. That saved our city a considerable amount of placement expense. We later decided to sell some of the bonds and some of our customers who were aware of the fact that we had bought all of them and wanted some of them approached us to buy some. We were told that we could not sell them because in essence that would be underwriting and we are prohibited by law from underwriting municipal revenue bonds. We can participate in underwriting municipal general obligation bonds, we can hold them in our portfolio, we do hold them in our portfolio. We can hold municipal revenue bonds in our portfolio, but we can't underwrite them. It seems to me to be an anamoly, not too dissimilar from many other situations which really are counterproductive not only from our customers' standpoint but for the entire community's standpoint.

I think allowing banks to underwrite municipal revenue bonds would not only increase the number of potential underwriters but it would widen the market for bonds, and both of these should be beneficial in their effect because they would tend to lower the cost of the bond issuance to the city and eventually the cost to the taxpayers.

Senator GORTON. Mr. Anderson, your 10 minutes are up. If you will summarize, please, I would appreciate it.

Mr. ANDERSON. All right. Basically, we also feel that in the underwriting situation we should be allowed to underwrite loans or security-backed loans, securitization of bond-backed by mortgage bonds has been an extremely successful market in the United States. There are over $400 billion of them in existence at the end of the year. We think that there are other areas that could be quite easily utilized by a bank such as ours.

We see some tremendous changes involving the financial services industry. We think that the evolving integration of the services industry presents some great opportunities for us to have financial products that are tailored to meet our customers' needs. But to take advantage of that, Congress needs to remove the restrictions which prohibit us from participating as equals in the areas of insurance and securities and real estate.

Basically, we feel that removing those restrictions would provide for more competition, provide us an opportunity to compete as equals and overall benefit not only our customers but the entire consumer public.

Thank you.

[The complete prepared statement follows:]

STATEMENT

OF

LYNN L. ANDERSON
PRESIDENT AND CHIEF EXECUTIVE OFFICER
FIRST NATIONAL BANK
LAWRENCE, KANSAS

BEFORE THE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

MAY 7, 1986

Mr. Chairman and members of the Committee, I am Lynn Anderson, President and Chief Executive Officer of First National Bank in Lawrence, Kansas. I appreciate this opportunity to share with you my perspective on the market for financial services and on the need to redefine the role of commercial banks.

Let me tell you a little about my community. Lawrence, Kansas has a population of about 60,000 and lies just west of Kansas City. We have four local banks, four S&Ls, seven credit unions and eight finance companies; Citibank and Norwest bank both have offices in our area. But competition for the financial business of our customers is not limited to these traditional players. For example, Dean Witter, a subsidiary of Sears and IDS, a subsidiary of American Express, both have offices in my building. These firms can and do offer combinations of financial products and services tailored to the needs of my customers, while my bank is tied by regulatory restraints which prevent our delivery of similar financial packages.

Mr. Chairman, as you and this Committee know, the environment for banks has changed dramatically over the past 10 years. Technological advances, especially in the fields of data processing and communications, have resulted in the creation of new services and have affected which institutions can most efficiently produce and deliver these services. For example, improvements in computer capability promoted the use of money market funds by lowering the transactions cost of handling large volumes of small investments. Another example is the development

of computerized mortgage networks which allow potential home buyers to shop nationwide for the type of mortgage best suited to their individual needs.

Significant demographic shifts have changed the financial service needs of our customers. For example, as the huge baby boom generation reached its 30's, we saw a tremendous increase in the demand for housing finance. As the baby boomers near 40, their demand for investments designed for retirement can be expected to grow.

The economic volatility of the past 10 years has also contributed to changing the types of services demanded by our customers. Bank depositors who saw the value of their fixed rate deposit investments eroded by inflation are no longer content to put money in a savings account and forget it. They have become increasingly sophisticated in their choices of financial instruments, seeing the need to diversify their savings to balance risk and return. I believe this is a positive, healthy development; consumers should take an active role in the management of their savings and investments.

My bank is currently involved in developing a financial planning service that we hope to provide not only to our trust accounts, but also to our bank customers. We believe that a key financial need for most consumers is advice -- advice on how each individual customer can use the financial services system to his best advantage.

I am a small businessman operating a small bank. We have a good rapport with our customers. This relationship, plus our

knowledge of our own local market and our expertise in financial matters, make us uniquely qualified to help customers develop a financial plan. This service would be useful to those customers who have wealth they need to protect. But it is equally important to those who are just starting out and need to develop a plan to protect their family, to begin providing for retirement and to accumulate savings and investments for such future needs as a college education for their children.

The frustrating part of this process is that our bank cannot provide most of the services we would include in a financial plan. For example, a financial plan for a young family would probably include life insurance and annuity products banks cannot sell. Insurance products are an important tool for risk management as well as savings for consumers. In many cases, it would be more convenient and perhaps less expensive for our customers to be able to purchase insurance products directly through the bank. Certainly it would be advantageous to allow consumers this option.

Another important element in a consumer financial plan is mutual funds, which banks cannot sponsor and distribute. We can, of course, offer collective or pooled investment funds for our trust customers. Our bank's trust department has provided this service for years. We have many bank customers who would like us to manage their investment funds in a similar efficient way, but who do not have or need a trust relationship with us. We currently have no legal way to satisfy these customers.

On the other hand, the Dean Witter office located in our building can offer full service securities brokerage and mutual funds, a full line of insurance products through the Sears Financial Network and Allstate Insurance, real estate brokerage and equity participations through Coldwell Banker, and insured deposits through Sears Savings Bank, along with a variety of other bank-like products.

I have no doubt that many of my customers find these packages of financial services attractive, and I can see no reason why they shouldn't have the opportunity to purchase them. But, Mr. Chairman, it is discouraging to watch my customers walk out of my bank to a Dean Witter or an IDS to get what they want. And once these customers leave the bank, it will be very difficult for me to get them back.

One recent example of our inability to meet our customers needs is in the IRA market. This year my bank aggressively promoted our IRA deposit instruments. In spite of our heavy promotion, we had a zero net gain in IRA deposits; without our active marketing program, I have no doubt we would have lost funds. Our customers, like customers across the country, seemed to favor annuities and mutual funds this year, products that we can't directly participate in. To help fill these gaps, we now make the mutual fund shares of Federated Securities, Inc., a subsidiary of Aetna Life and Casualty Co., available to our customers, and we have considered an arrangement with an insurance company to put a kiosk in our lobby. It is certainly

not clear that this is the most efficient way to provide these services, but we currently have no choice.

What we would like, Mr. Chairman, is to have the choice of how to best serve our customers. Banking is a competitive, service oriented business. We are convinced that to be successful, our bank must emphasize the quality of treatment of our customers as well as the quality of the products sold. We feel that we lose a substantial measure of control over these important elements by having to contract with outside firms to provide the services our customers need and which we could provide.

Real estate brokerage is a natural extension of the types of financial services we would like to offer our customers. Buying a house is the biggest single purchase most consumers make. Often our customers come to us for advice on what kind of housing they can afford, how to finance the purchase and for help in evaluating the property. About 15% of our loan portfolio is currently held in residential mortgage loans. In addition, we originate and sell a substantial volume of mortgages. In other words, we are involved in each step of the transaction, but must send our customers to another firm for brokerage services.

Let me give you another example of how legal restrictions prevent my bank from helping our community. On one occasion, we bought an entire issue of local municipal revenue bonds which saved our city considerable placement expense. When we later decided to sell some of the bonds, some of our customers expressed an interest in purchasing them; but we couldn't sell

them directly because that would be underwriting. We can participate in underwriting municipal general obligation bonds, and we hold both general obligation and revenue bonds in our portfolio - - yet we are prohibited from underwriting revenue bonds. Surely this anomaly is counter productive from the community's perspective. Allowing banks to underwrite municipal revenue bonds would increase the number of potential underwriters and widen the market for bonds; both of these effects would be beneficial, tending to lower the cost of bond issuance to the city.

In addition, it would be advantageous to the community if banks were permitted to underwrite securities backed by loans we may hold in our portfolio. For example, we hold housing loans, student loans, consumer loans, small business loans; each of these loan categories could be packaged and sold as securities. The most striking example of securitization is mortgage backed bonds. The dollar volume outstanding of these securities in the national market amounted to about $400 billion by the end of 1985. The packaging and selling of other types of loans is just beginning, but there is every reason to believe that it will be as successful as it has been with residential mortgages. The securitization process increases the flow of funds and adds liquidity to the market. The result is a decrease in the cost of lending. But today, banks cannot underwrite securities backed by their own loans.

Let me sum up the situation as I see it. Our customers demand and deserve more efficient and convenient provision of

financial services. We see the evolving integration of the financial services market as a great opportunity to provide our customers with innovative products tailored to meet their needs.

To take advantage of this opportunity, Congress must act to remove the legal and regulatory restrictions which keep banks from participating as equals in the areas of insurance, securities, and real estate. The resulting boost to competition in these areas is quite likely to result in lower prices and increased convenience for consumers. But perhaps more important, the breaking down of outmoded structural barriers will unleash the creativity of the free market. Surely the greatest advances in consumer well being have come from changes in the nature of the products we buy and the ways they are made available to us. For example in the financial services area, not long ago there was no such thing as a homeowners policy, no-fault insurance, universal life insurance, discount brokerage, open lines of credit at banks for average folks, and direct deposit to mention just a few of the recent innovations. If the suppliers of goods and services are allowed to compete freely and fairly, consumers will benefit not only from lower prices and increased convenience but from new and better products and services.

Senator GORTON. Thank you.
Mr. Kinst.

STATEMENT OF THOMAS A. KINST, LAND OF LINCOLN SAVINGS & LOAN, ILLINOIS

Mr. KINST. Thank you, Mr. Chairman.

I would like to take this opportunity to thank the members of the Senate Banking Committee for their invitation to Land of Lincoln Savings & Loan and its financial services network to address a very important topic to both consumers and providers of financial services. Essentially, the topic is what customer service or combination of services will allow savings and loan associations to remain an integral part of the financial industry.

Land of Lincoln is an $800 million asset size, publicly held stock, State-chartered, FSLIC-insured savings and loan operating without a holding company. Our financial services network serves the Chicago metropolitan area with 25 offices and the rural downstate Illinois market with 8 offices. On March 31, 1986, its equity-to-assets ratio was 6.31 percent and its liquidity ratio was 26.6 percent.

I would like to focus my comments to this subcommittee on the role of Land of Lincoln and its customers in the financial services arena. In that regard, I would like to review some basic points. Land of Lincoln's most important asset is its customer base. The value of this asset changes daily as public confidence in the banking system changes. The value of this asset is further affected by how well Land of Lincoln is able to deliver its products and services to all its varied customers in a competitive marketplace. And, last, the value of this asset is affected by the legal and regulatory requirements imposed on the operations of Land of Lincoln.

All these factors impact our ability to serve consumers with viability and profitability in order to provide these services.

EXPANDED SERVICES PROVIDED

From its roots as a savings and loan, started in 1916, Land of Lincoln has added various products and services to assist its customers as their needs evolved. Over the years, we expanded its role from the savings and loan by adding the following services: full securities brokerage through an acquisition of a registered broker-dealer, real estate brokerage and franchising, title insurance, trust, tax preparation, land development, home construction, real estate syndications, and other services to become a multifaceted financial services provider. I have included a brochure of our financial service network with my written statement for your review. Our overall strategy is based on our philosophy of providing total service and convenience to all consumers.

Land of Lincoln developed its basic financial distribution and delivery system through its branches and subsidiary companies. Therefore, by maximizing utilization of office space and increasing productivity of our counselors by effective cross-marketing efforts, we have found that it is cost effective for both Land of Lincoln to provide and for its customers to use new or previously unoffered products and services. Other organizations with nondepository distribution and delivery systems are also becoming providers of fi-

nancial services. We believe that any type of national company with a distribution and computer network will be a future competitor. Backed by many surveys, consumers have had more trust and confidence in their financial institutions than in other organizations. Therefore, it should be more effective and a natural extension for a financial institution to increase its relationship with a customer than for a nonfinancial institution. Studies have also indicated that for every added service utilized by a customer, the retention period of that account increases.

I think we're doing things right because just recently we saw a survey by Arthur Anderson which supports our logical program. The survey was basically comparing consumer preferences of needs and services that they felt were important and also it reported the respondents or the banks rankings. It's interesting to note at the current bank the consumer survey participants ranked No. 1 convenience; No. 2, prior or present relationship; No. 3, reputation of the institution; No. 4, variety of products and services offered; and No. 5, rates and fees.

For criteria for a new bank, convenience still remains the No. 1 most important factor. Variety of products and services offered rank No. 2; safety of the institution No. 3—actually, they were tied 2 and 3—rates and fees were 4; and quality of service and personnel was 5.

Let me give you an example of what happened just several months ago. A customer came into our chairman's office and said that he saw that we were in the real estate brokerage business in our Lincoln Log publication and that he was moving down to Florida and asked if we could help him out. So our chairman said, yes, we could and he picked up the phone and he called our Land of Lincoln partners real estate brokerage company and talked to their referral department and got a name of an agent down in Florida. We also secured a listing on his building in Berwyn. The man went down to Florida and he did buy a home down there. We eventually sold the property. We secured the title insurance and the insurance and we also made the mortgage on his present building in our location.

This customer came back and visited with our chairman later on after the closing and he said, "Frank, I have $88,000 from closing and you have all my certificates and other savings programs. What can you do for me?" He took them over to our stock brokerage company's offices right in the building and they gave him investment advice and he ended up buying $88,000 worth of bonds.

Another example of providing convenience for consumers is when anyone transfers from one State to Illinois and comes into our real estate brokerage business, they have to reestablish all their account relationships from the previous location. The first thing they have to look for, of course, is a real estate broker. Then when they find a house they have to get a mortgage, they have to get a title to close, they have to have insurance to close. They also have to come up and open a new checking account, maybe transfer their savings and possibly a broker account and maybe even set up a land trust.

We feel that we can provide those services conveniently and cost effectively for those customers.

As far as the public confidence factor, with the many highly publicized instances of financial minicrises—the Ohio and Maryland thrift crises, the takeover of Continental Bank by the FDIC, the foreign, energy and farm bank problems—consumers are more wary of losing their life's savings even if such an institution is federally insured. It is, therefore, important that financial institutions be well-capitalized and, more importantly, be able to compete effectively in the marketplace. If not, the larger corporations providing cost-effective, sophisticated marketing techniques will raid profitable customers from the noncompetitive thrifts. By not being able to provide as many of the services that a consumer requires, depository institutions—be they banks or thrifts—risk having their customer base eroded, and likewise their profit and capital.

Land of Lincoln has double the Federal net worth requirement and five times the liquidity requirement. We are doing our part in maintaining consumer confidence in the banking system.

NATIONWIDE BANKING AND FINANCIAL SERVICES ARE ALREADY HERE

We feel that nationwide banking and financial services are already here and, therefore, efforts to further restrict or reregulate thrift institutions is suicide. You can't unscramble scrambled eggs. In fact, further deregulation should be considered to give all the thrifts, both State and Federal, the right to be able, if they so desire, to create their own financial and real estate services network, whether it be one office, statewide or even nationwide. Competition is good for business and good for the consumer. Although the trend seems to be to automate and depersonalize the financial function, there is still a significant share of the consumer market that prefers to deal with people. These people need other people's help. As there are more technological and financial developments, there will be a greater need for community financial institutions that provide the personal touch—real people that a consumer can see, ask questions of, and receive prompt and courteous professional responses from.

The concept of a community financial institution is still alive and well. Land of Lincoln takes pride in its Lincoln Log, its quarterly in-house publication sent to over 300,000 households in its market area. It also has a strong belief in consumer education, as evidenced by its seminars on taxes and investments, home buying and selling, estates and wills, and other financially related topics.

Because our customers are dynamic, that is their ages and financial needs continue to change almost daily, we must be ready to offer as many services as possible, whether or not all the services are used by everyone. To continue to offer these services, some of which are not presently cost justifiable, we have to remain financially viable. We must be able to retain our present customer base and attract new customers. By providing a variety of financial services to satisfy its customers' needs, Land of Lincoln believes that we can offer these services cost effectively and conveniently.

Many of these people may never have had access to certain kinds of financial services and products, so Land of Lincoln provided it. Land of Lincoln also decided that full-service brokerage rather than discount brokerage was in the best interests of its customers.

In an increasingly complex financial world, more and more people understand less and less about their financial alternatives, so a discount broker who only executes transactions does not provide the service that a relatively unsophisticated consumer requires.

As far as legal and regulatory requirements, Land of Lincoln has always believed it was in the best interests of consumers in general and its customers in particular to provide the greatest amount of products and services as it legally could do so. Since Lincoln's philosophy is full service——

Senator GORTON. Mr. Kinst, your 10 minutes is up. At this point your full written statement will be included in the record as if read in full.

Mr. KINST. OK.

[The complete prepared statement follows:]

STATEMENT OF
THOMAS A. KIRBY
BEFORE THE
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER AFFAIRS
OF THE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
May 7, 1986

I would like to take this opportunity to thank the members of the Senate Banking Committee for their invitation to Land of Lincoln Savings and Loan and its Financial Services Network to address a very important topic to both consumers and providers of financial services. Essentially, the topic is what customer service or combination of services will allow savings and loan associations to remain an integral part of the financial industry.

Land of Lincoln is an $800 million asset size, publicly held stock, state-chartered, FSLIC-insured savings and loan operating without a holding company structure. Our financial services network serves the Chicago metropolitan area with 25 offices and the rural downstate Illinois market with 8 offices. On March 31, 1986, its equity to assets ratio was 6.31% and its liquidity ratio was 26.6%.

I would like to focus my comments to this Committee on the role of Land of Lincoln and its customers in the financial services arena. In that regard, I would like to review some basic points. Land of Lincoln's most important asset is its customer base. The value of this asset changes daily as public confidence in the banking system changes. The value of this asset is further affected by how well Land of Lincoln is able to deliver its products and services to all its varied customers in a competitive marketplace. And, lastly, the value of this asset is affected by the legal and regulatory requirements imposed on the operations of Land of Lincoln.

From its roots as a savings and loan, started in 1918, Land of Lincoln has added various products and services to assist its customers as their needs evolved. Land of Lincoln first expanded its role from a savings and loan by adding full-service securities brokerage through an acquisition of a registered broker/dealer. This was followed by real estate brokerage and franchising, title insurance, trust, tax preparation, land development, home construction, real estate syndications, and other services to become a multi-faceted financial services provider. Our overall strategy is based on our philosophy of providing total service and convenience to all consumers.

Land of Lincoln developed its basic financial distribution and delivery system through its branches and subsidiary companies. Therefore, by maximizing utilization of office space and increasing productivity of our counselors by effective cross-marketing efforts, we have found that it is cost effective for both Land of Lincoln to provide and for its customers to use new or previously unoffered products and services. Other organizations with nondepository distribution and delivery systems are also becoming providers of financial services. We believe that any type of national company with a distribution and computer network will be a future competitor. Backed by many surveys, consumers have had more trust and confidence in their financial institutions than in other organizations. Therefore it should be more effective and a natural extension for a financial institution to increase its relationship with a customer than for a nonfinancial institution. Studies have also indicated that for every added service utilized by a customer, the retention period also increases.

PUBLIC CONFIDENCE

With the many highly publicized instances of financial mini-crises (the Ohio and Maryland thrift crises, the takeover of Continental Bank by FDIC, the foreign, energy and farm bank problems), consumers are more wary of losing their life's savings even if such savings are with a federally insured financial institution. It is, therefore, important that financial institutions be well-capitalized and, more importantly, be able to compete effectively in the marketplace. If not, the larger corporations providing cost-effective, sophisticated marketing techniques will effectively raid profitable customers from the noncompetitive thrifts. They are leaving the more difficult and, many times, less financially rewarding and time consuming function of face-to-face customer relations to local community financial institutions. By not being able to provide as many of the services that a consumer requires, depository institutions -- be they banks or thrifts -- risk having their customer base erode, and likewise their profit and capital.

Land of Lincoln has double the federal net worth requirement and five times the liquidity requirement. We are doing our part in maintaining consumer confidence in the banking system.

GENERIC PRODUCTS VERSUS PERSONALIZED SERVICE

While McDonald's has made buying a hamburger a generic item not only nationally, but also internationally, money is a very personal thing with most people. Dealing with a person's financial welfare is still very different than buying a hamburger. We are charged with protecting our customer's life savings.

More financial products are being converted to generic national instruments. We acknowledge that there are monetary and nonmonetary benefits to consumers in having a national or even international credit card, or being

able to withdraw cash from an ATM (Automated Teller Machine) anywhere in a city or state or in the nation, or being able to obtain the highest certificate rate or the lowest possible mortgage loan rate through a nationwide telerate type operation. These are some of the benefits that cost-effective high technology produces in our modern banking world. These and other innovations have made a positive contribution to our society.

Because nationwide banking and financial services are already here, we feel that efforts to further restrict or re-regulate thrift institutions is suicide. You can't unscramble scrambled eggs. In fact, further deregulation should be considered to give all the thrifts, both state and federal, the right to be able, if they so desire, to create their own financial and real estate services network, whether it be one office, statewide or even nationwide. Competition is good for business and good for the consumer. Although the trend seems to be to automate and depersonalize the financial function, there is still a significant share of the consumer market that prefers to deal with people. These people need other people's help. As there are more technological and financial developments, there will be a greater need for community financial institutuons that provide the PERSONAL TOUCH -- real people that a consumer can see, ask questions of, and receive professional prompt and courteous responses from.

The concept of a community financial institution is still alive and well. Land of Lincoln takes pride in its Lincoln Log, a quarterly in-house publication sent to over 300,000 households and customers. It also is a strong believer in consumer education, as evidenced by its seminars on taxes and investments, home buying and selling, estates and wills, and other financially-related topics.

Because our customers are dynamic, that is their ages and financial needs continue to change almost daily, we must be ready to offer as many services as possible, whether or not all the services are used by everyone. To continue to offer these services, some of which are not presently cost justifiable, we have to remain financially viable. We must be able to retain our present customer base and attract new customers. By providing a variety of financial services to satisfy its customers' needs, Land of Lincoln believes that old-fashioned advertising, that is word-of-mouth advertising and professional service and effective cross-sell marketing techniques, will provide it with new customers. This process will allow Land of Lincoln to offer additional services and offer these services cost-effectively.

Many of these people have never had access to certain kinds of financial services and products. A factory worker does not generally play golf at a stockbroker's private country club. Yet, that factory worker should be able to have convenient access to the kinds of financial services a stockbroker provides. Land of Lincoln decided that many of its customers did not have such access, so Land of Lincoln provided it. Land of Lincoln also decided that full-service brokerage rather than discount brokerage was in the best interests of its customers. In an increasingly complex financial world, more and more people understand less and less about their financial alternatives, so a discount broker who only executes transactions does not provide the service that a relatively unsophisticated consumer requires. I would suggest that even sophisticated consumers need the services of a full service stockbroker or investment adviser.

LEGAL AND REGULATORY REQUIREMENTS

Land of Lincoln has always believed it was in the best interests of consumers in general and its customers in particular to provide the greatest amount of products and services as it legally could do so. To this end, Land of Lincoln switched charters from state to federal in 1958 and back to state in 1978, and then converted from a mutual to stock organization in 1979 so it can be in the financial and legal position to provide the services its customers require. The dual system of federal and state chartering allows financial institutions to be responsive to the needs of the marketplace they serve.

The Garn-St Germain Act of 1982 did provide additional powers to thrifts but the powers did not cause the problems, rather economic conditions and irresponsible managements or worse caused the problems while strong managements used the powers as they were intended, for the good of the consumer and the thrift. We cannot allow the majority of the thrift industry and consumers to suffer for the actions of the small minority, or economic conditions beyond their control. The industry needs further deregulation not reregulation to maintain equilibrium and viability, to provide complete and competitive services to consum

We must be free to compete with anyone. We were never afraid of competition and have always believed in providing the best service to all our customers that the free marketplace demands.

SUMMARY

I have submitted with my written testimony a brochure describing our Financial Services Network and also a copy of our Lincoln Log.

At this time, I would be pleased to entertain any questions that you may have.

Senator GORTON. I do have some questions for you.

First, I'd like each of you to comment on Senator Proxmire's reference to two studies which indicate at least in those cases that consumers are much more interested in better service than they are in new products or new services.

Do you have any comment on those studies and on what you have found in the businesses which each of you runs?

Mr. KINST. I'll start. We basically don't go by surveys. We just use our intuition. We've been in the business for many years. Our business has grown. We have remained profitable. It is pleasing to note that the survey that I referred to does contradict some of those areas; in fact. The survey surprised us as to the points of safety of the institution and reputation of the institution.

But it clearly shows, although this is a small ranking and with banks, convenience—that's unanimous I believe in any survey. Prior or present account relationship is certainly very valid in the current bank affiliation. However, that does not even show on the new bank. The reputation and safety applies as No. 3; and variety of products and services in selection of a new bank would be No. 2 compared to No. 4 in the current bank. And yet rates and fees are fifth and fourth.

Senator GORTON. Mr. Anderson.

GOOD SERVICE A PREREQUISITE

Mr. ANDERSON. Well, mine would be the same. It's very similar to the restaurant business. You can have a wonderful menu and a wide array of entrees, but if you can't provide the service you're not going to have the customers. So I think it goes without saying that you're going to have to provide good service or you won't have customers.

The point is, where do you go after you provide the good service and what kind of products do your customers want?

Our research in our marketplace, which is both statistical and experience, is that customers will buy new products from us. They bought new products in the past and they will continue in the future.

There is a demand for good service everywhere. They will make a judgment as to whether they're getting that, but they will also make a judgment as to whether they can get both the good service and the new products someplace else.

Senator GORTON. Is the consumer advantaged or disadvantaged by the nonbank bank loophole?

Mr. ANDERSON. They are probably advantaged to some extent because there's another competitor for their business. The ones that are really disadvantaged are those of us that are in the traditional roles.

Mr. KINST. I would have to concur with that.

Senator GORTON. Garn-St Germain created the money market deposit account in order to allow for competition with money market foundations where banks might sell a money market, life insurance, a life annuity, as part of the program. They might provide some type of investment management of equities, debt securities other than CD's and that type of thing.

I think the situation is going to evolve where we basically treat customers in their total relationship from a financial standpoint. That's really what they need. They don't want part of their program treated here and part treated elsewhere any more than you want that when you go to have a physical by a physician. You want your total person analyzed. You want your total needs and your total well-being served. And I think that's really what the point is, the total financial well-being of the client or the customer.

Senator GORTON. Mr. Kinst.

Mr. KINST. It was the first effort to indicate the acceptance or the need to provide that for our customers, realizing that there are other needs and hopefully that we will see more liberalization for these other accounts to follow that lead.

Senator GORTON. What hours and days are you open, Mr. Anderson?

Mr. ANDERSON. For teller services we're open 9 to 6, 5 days a week and 9 to noon on Saturdays. So we're open basically for business a total of 6 days. We have teller services and loan officers available during that period. And in a community bank we're available by phone call at home and so forth. So it's full service.

Mr. KINST. We are open Mondays, Tuesdays, half day on Wednesdays, Thursdays, Friday nights and Saturdays.

Senator GORTON. One night a week?

Mr. KINST. Yes, Friday night. In some cases, our drive-ups are open 5 days a week. We have different hours for different locations.

Senator GORTON. Would your customers be more benefited by your being open more widely in the evening or by new services?

BETTER SERVED BY MORE PRODUCTS

Mr. ANDERSON. Our customers would be more served and better served by more products. We find in our surveys and in talking to customers they can get to the bank if they need to. It's also, as I say, available by phone. Many people don't come into the bank. They transact business by phone or by mail. In a community our size, distance is not a real factor. So it's an area that we're concerned about and constantly watch and we've expanded our hours twice in the last 3 years.

Mr. KINST. I would also say products and services. Basically, our customers have over 600 locations where they can have access to their cash or accounts through a PLS system in the 24-hour supermarkets and service stores.

Senator GORTON. Mr. Anderson, do you agree with Mr. Kinst's surveys that fees for essential bank services are a relatively low priority with your customers?

Mr. ANDERSON. Yes, that's been our experience, if they are explained. Customers do not object to fees if they are explained.

Senator GORTON. Are your fees competitive?

Mr. ANDERSON. Yes.

Mr. KINST. Oh, definitely, yes. In fact, we're probably on the low end.

Senator GORTON. What about check hold periods?

Mr. ANDERSON. Very competitive. We find it's a nonissue in our area. Far less than 95 to 96 percent of the checks in our bank are

held for any period of time. They are really only held on the new accounts and it's just not an issue.

Again, I think it's a matter of explaining to the customer. If the customer has information on it, they seem satisfied with it. It's a nonissue in our marketplace.

Mr. KINST. We are on the lower end of the scale on that also. It's interesting to note that there's another alternative to check holds. People can, and they are doing so with much more frequency, have their payroll checks deposited directly to the institutions, which removes all check holds. They are immediately accessible.

Senator GORTON. I want to thank both of you for being here today and for helping us kind of learn more about our responsibility.

Mr. ANDERSON. Thank you.

Mr. KINST. Thank you.

Senator GORTON. The meeting is adjourned.

[Whereupon, at 11:10 a.m., the hearing was adjourned.]

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